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No. ——— OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

SHELL OIL COMPANY,
Petitioner,

v.

STUDIENGESELLSCHAFT KOHLE M.B.H.,
Respondent.

Petition for Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

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PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

Where a patent licensee challenges the validity of the licensed patent as authorized by *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), and where the Court has found the relevant patent claims invalid, is that invalidity a complete defense to all royalty damages or may the licensor still seek damages for breach of contract for past royalties due on processes allegedly covered by such claims from the date of the alleged breach until the date that the licensee first challenged the validity of such claims?

LIST OF PARTIES AND RULE 29.6 STATEMENT

The parties to the proceeding in the United States Court of Appeals for the Federal Circuit were petitioner Shell Oil Company and respondent Studiengesellschaft Kohle M.B.H. For purposes of S. Ct. R. 29.6, Shell Oil Company states that its parent companies or nonwholly-owned subsidiaries are as follows: (1) Shell Transport and Trading Company PLC and (2) Royal Dutch Petroleum Company.

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PETITION FOR WRIT OF CERTIORARI

Shell Oil Company ("Shell") petitions that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Federal Circuit in this case with respect to that court's resolution of the certified legal question raised in Shell's cross-appeal No. 96-1200.

PREVIOUS OPINIONS IN THE CASE

The Federal Circuit's opinion is reported at *Studiengesellschaft Kohle M.B.H. v. Shell Oil Co.*, 112 F.3d 1561 (Fed. Cir. 1997), and is found at Petitioner's Appendix ("App.") 1a-15a. The district court's order granting summary judgment of invalidity of claims 1-6 and 14 of U.S. Patent No. 4,125,698 ("the '698 patent"), dismissing the infringement claims of Studiengesellschaft Kohle m.b.H. ("SGK") as moot, and ordering that trial proceed on SGK's breach of contract claim based on its license of the '698 patent to Shell is found at App. 16a-27a. The district court's order denying Shell's motion for reconsideration and denying SGK's motion for final judgment is at App. 28a-30a.

The district court's final judgment under Fed. R. Civ. P. 54(b) on the patent invalidity and infringement issues is found at App. 31a-32a. On the same day, the district court issued an order certifying the following question of law for interlocutory appeal under 28 U.S.C. § 1292(b):

> Where the Court has found the relevant patent claims invalid, may the Licensor recover damages for breach of contract for past royalties due on processes allegedly covered by such claims, from the date of the alleged breach until the date that the Licensee first challenged the validity of such claims?

App. 33a. The Federal Circuit's unpublished order granting Shell's petition for permission to appeal the certified question and granting SGK's motion for consolidation of the parties' appeals is found at App. 35a-38a. The ques-

tion presented by this petition seeks review of the Federal Circuit's resolution of the certified question to permit a licensor to use contract law to seek past royalties after the licensed patent is held invalid.

JURISDICTION

The decision of the Federal Circuit issued on May 5, 1997. App. 1a. The court of appeals denied SGK's timely combined petition for rehearing and suggestion for rehearing *in banc* in an order dated June 27, 1997. App. 39. A motion by Shell seeking a stay of the mandate pending disposition of this petition was later denied by the court of appeals.

The jurisdiction of the district court was invoked under 28 U.S.C. § 1338(a). The jurisdiction of the court of appeals was invoked under 28 U.S.C. § 1292(a)(1) and (c)(1) with respect to the certified legal issue and under 28 U.S.C. § 1295(a)(1) with respect to the patent invalidity and infringement issues. This Court has jurisdiction to entertain the present petition under 28 U.S.C. § 1254(1).

STATUTORY PROVISION INVOLVED

This petition raises an important issue of law relating to competing policies under federal patent law and state contract law, as identified in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), with respect to a patent licensee's liability for past royalties under a patent license after the licensee successfully invalidates the licensed patent during litigation with the licensor.

In the nearly 30 years since *Lear*, a number of federal courts have deviated from its express teachings by creating or accepting a rule of law that the invalidity of a licensed patent only allows a licensee to avoid liability for unpaid royalties that accrue after the licensee gives notice to the licensor that the licensed patent is believed to be invalid. Because Shell seeks a writ of certiorari to

review the Federal Circuit's decision in this case to adopt that rule as its precedent, there is no statutory provision directly applicable to this petition.

STATEMENT OF THE CASE

A. *The Parties' Patent License Dispute*

The '698 patent is part of a family of patents filed by Karl Ziegler and various co-inventors (collectively "Ziegler") and relates to the polymerization of olefins, such as ethylene and propylene, to produce plastics. Plaintiff-respondent SGK is the licensing arm of the Max-Planck Institute for Coal Research, a German research and educational organization, to which the Ziegler patents were assigned.

In 1974, SGK and Shell entered into a license agreement whereby Shell was licensed to polymerize propylene under various U.S. patents owned by SGK in exchange for a running royalty on sales of the resulting polypropylene. App. 50a-58a. One of the licensed patents was U.S. Patent No. 3,113,115 ("the '115 patent"), which claimed a catalyst useful for polymerizing olefins, including propylene. In 1978, the '698 patent issued, claiming a polymerization process using the same polymerization catalyst set forth in the '115 patent. While Shell was licensed to practice the process claimed in the '698 patent under the agreement, issuance of the '698 patent meant that Shell's royalty obligations to SGK would not end with the expiration of the '115 patent, but would extend for an additional 15 years.

In 1979, Shell renegotiated its license with SGK, modifying the terms of the 1974 agreement to receive a paid-up license to produce 450 million pounds of polypropylene per year, and to pay a 1.0% running royalty on any sales over that amount. App. 59a-61a. In 1987, in settlement of a dispute over royalties owed under the existing license agreement, the parties again modified the license, raising Shell's running royalty rate to 1.5%. App. 62a-64a. As

amended in 1987, the parties' license agreement related only to the production of polypropylene pursuant to the claims of the '698 patent. App. 62a.

Under the 1987 agreement, Shell did not owe royalties on polypropylene produced by a process not covered by claim 1, nor would such polypropylene count against Shell's paid-up capacity. The agreement also provided that Shell was to provide SGK with annual reports as to "the amount of Polypropylene produced which [Shell] considers as falling outside of the license and . . . provide SGK, in confidence, with sufficient information to allow SGK to independently evaluate whether or not said production is, in fact, outside of the scope of the license." App. 63a. Later, Shell assigned one third of its paid-up capacity to another company as allowed by the license. *Id.* at ¶ 5.

Subsequently, Shell began producing polypropylene in 1987 using a new process, primarily at a plant in Seadrift, Texas ("the Seadrift process"), while still operating its older polypropylene process at a different plant. Shell has consistently insisted that the Seadrift process is not covered by any claims of the '698 patent. Accordingly, Shell never paid any royalties on polypropylene produced by the Seadrift process, but did continue to pay all royalties that were due on its older process when its use of the older process exceeded its paid-up capacity.

When SGK inquired about the production levels on Shell's royalty reports, Shell responded by providing SGK with sufficient information to show that the Seadrift process was not covered by any claims of the '698 patent. SGK, however, refused to agree that the Seadrift process was not covered by any '698 patent claims and demanded payment for past royalties allegedly due for the Seadrift process. Ultimately, because Shell refused to pay royalties for its Seadrift process, SGK purported to terminate the license agreement, and filed the present action in 1993.

SGK's complaint asserted that Shell breached the license agreement by not paying all royalties owed for its produc-

tion of polypropylene and that Shell's breach enabled SGK to treat such polypropylene production as patent infringement. App. 40a-41a. SGK sought damages for breach of contract (for the period between 1987 and the termination of the license) and for infringement of the '698 patent (for the period after the license termination). *Id.* Shell counterclaimed for a declaratory judgment that the license agreement had not been breached and was not properly terminated, and that the '698 patent was invalid, unenforceable, and not infringed by Shell's polypropylene operations. App. 44a-49a.

B. *The District Court Proceedings*

The '698 patent emerged from a series of patent applications prosecuted in the U.S. Patent Office over a period of 23 years. The application that resulted in the '698 patent was filed on October 29, 1958. Because that application combined the distinct disclosures of two other prior Ziegler applications separately filed in January and June of 1955, the combined application for the '698 patent was a continuation-in-part application with respect to each of the individual parent applications. *See* App. 2a-3a (citing *Studiengesellschaft Kohle m.b.H. v. Northern Petrochemical Co.*, 784 F.2d 351, 352 (Fed. Cir.), *cert. dismissed*, 478 U.S. 1028 (1986)).

As SGK eventually conceded, claims 1-6 and 14 of the '698 patent cover a process disclosed in Belgian Patent No. 538,782 ("the Belgian patent"), patented on December 6, 1955, more than one year before the filing of the application resulting in the '698 patent. *See* App. 3a. Under 35 U.S.C. § 102(b), the Belgian patent is thus a statutory bar that invalidates those claims unless they were entitled to the earlier filing date of one of the parent applications under 35 U.S.C. § 120.

After discovery closed, Shell filed motions for summary judgment that claims 1-6 and 14 of the '698 patent were invalid under 35 U.S.C. § 102(b) in view of the

Belgian patent, and that the '698 patent was not infringed. In opposing Shell's motions, SGK asserted additional claims 7, 9-12, and 15 of the '698 patent against different processes used by Shell to make polybutylene, but made no mention of any other '698 patent claims.

When the parties convened for a scheduled pretrial conference, the district court distributed a "Tentative Order" granting Shell's motion for summary judgment of invalidity and dismissing SGK's claims for patent infringement and breach of contract. In objecting to the tentative order, SGK raised eleventh hour arguments not previously presented. In particular, SGK argued that, even if the district court held claims 1-6 and 14 of the '698 patent invalid, the court could not dismiss SGK's breach of contract cause of action, because invalidity was a defense only for the period after the licensee informs the licensor that it believes the patent is invalid.[1]

On August 31, 1995, the district court entered an order granting Shell's motion for summary judgment of invalidity, holding that neither of the Ziegler parent applications alone described the invention of the '698 claims at issue and that section 120 did not permit the combination of two earlier disclosures as a means to acquire an earlier filing date. App. 19a-24a. The district court also dismissed SGK's infringement cause of action, stating that SGK's infringement assertions against Shell's polybutylene processes were not properly before the court, and dismissed Shell's noninfringement summary judgment motion as moot. App. 24a.

With respect to the issue raised by this petition, the district court reversed its tentative ruling to dismiss SGK's

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[1] On the invalidity issue, SGK only complained that the district court was applying the wrong legal standard. SGK also argued against dismissal of its infringement cause of action because it was asserting additional claims of the '698 patent (including, for the first time, claim 13) and because SGK had also properly asserted an infringement claim against Shell's polybutylene operations.

contract claim, ruling instead that federal law did not prohibit a licensor from seeking past royalties even though the relevant underlying patent claims were invalid. App. 25a-26a. This ruling thus mandated that a trial proceed on SGK's breach of contract cause of action even though the patent claims asserted by SGK against Shell's polypropylene processes had already been held to be invalid as a matter of law. App. 26a; 28a-30a.

Upon a joint motion, the district court entered a final judgment under Fed. R. Civ. P. 54(b) dismissing SGK's infringement cause of action. App. 31a. Concluding that the question of whether the invalidity of the relevant patent claims is a defense to an action seeking past royalties presented a controlling issue of law as to which there is a substantial ground for difference of opinion, the district court certified that issue for interlocutory appeal under 28 U.S.C. § 1292(b). App. 33a. The Federal Circuit then granted Shell's unopposed petition for leave to appeal the certified issue and consolidated it with SGK's appeal from the Rule 54(b) judgment. App. 35a-38a.

C. *The Federal Circuit Proceedings*

On its *de novo* review of the invalidity issue, the Federal Circuit agreed with the district court's holding that the disclosures of two earlier filed applications could not be combined to acquire an earlier filing date under 35 U.S.C. § 120, and that claims 1-6 and 14 were limited to the filing date of the '698 patent and were thus anticipated by the prior art Belgian patent. App. 5a-8a. On that basis, the Federal Circuit affirmed the district court's summary judgment of invalidity with respect to claims 1-6 and 14 of the '698 patent.[2] App. 8a.

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[2] The Federal Circuit also held that SGK had not expressly stated an intent to drop its assertion that claim 13 was infringed by Shell's polypropylene operations, and therefore remanded that issue because the district court did not provide an adequate reason for not ruling on that issue. App. 8a-9a. With respect to SGK's assertion that claims 7, 9-12, and 15 of the '698 patent were infringed by

Turning to the certified question of law that is the sole subject of this petition, the Federal Circuit began by stating that "[t]he record showed that Shell breached [its license with SGK] by producing polypropylene under the Seadrift process without either paying royalties or reporting the production as being outside of the license." App. 11a. It is clear, however, that such breach was only assumed by the Federal Circuit; otherwise, no remand would have been necessary on the contract issue.[3]

According to the Federal Circuit, if patent law and policy were set aside, the terms of the parties' license would obligate Shell to pay royalties on polypropylene produced in accordance with claim 1 of the '698 patent—regardless of the '698 patent's validity. App. 11a-12a. However, this Court's landmark decision in *Lear* had already settled that it was contract law, not federal patent policy, that was to be set aside when a licensor sought royalties under a license to an invalid patent. 395 U.S. at 670. In the Federal Circuit's view, this Court's elimination of licensee estoppel in *Lear* merely reflected "a past era of skepticism over intellectual property principles." App. 12a.

After giving lip service to *Lear*, the Federal Circuit then recited numerous of its own decisons that had distinguished *Lear* and unabashedly relied on them to avoid this Court's

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Shell's polybutylene operations, the Federal Circuit held that the district court abused its discretion by erroneously finding that SGK did not raise those claims until the joint pretrial order, and so remanded the alleged infringement by the polybutylene processes for further consideration. App. 10a-12a.

[3] As to a breach by failure to pay royalties on the Seadrift process, the Federal Circuit clarified that it was only "assuming that the Seadrift process infringes claim 1 of the '698 patent and thus fits within the terms of the license." App. 11a-12a. As to a breach by failure to report, it was later described by the court as "Shell's apparent breach of its duty to notify." App. 14a. In actuality, Shell's production from its Seadrift process was reported to SGK within 60 days of SGK's inquiry, so any alleged breach on that basis was fully cured as provided in paragraph VI(a) of the parties' 1974 license agreement. App. 54a.

teachings in *Lear* once again.[4] In particular, the court relied on its decision in *Diamond Scientific*, in which it reinstated the doctrine of assignor estoppel by distinguishing *Lear* as directed to validity challenges by licensees, rather than assignors. By so avoiding *Lear* in *Diamond Scientific*, and then using *Diamond Scientific* as controlling in this case, the Federal Circuit completed an improper end run around *Lear* that should be called back by this Court.

To the Federal Circuit, this case was just like *Diamond Scientific* because Shell's license had "produced significant benefits for the corporation and attested to the worth of the patent." App. 13a. The court then listed Shell's alleged "benefits" as being insulated from unlicensed competition, from investigations of infringement, and even from royalties until SGK's discovery of the Seadrift process. *Id.* Even though Shell did not seek or receive any protection of the license for its new Seadrift process, the Federal Circuit felt compelled by *Diamond Scientific*'s reasoning to conclude that it "must prevent the injustice of allowing Shell to exploit the protection of the contract and patent rights and then later to abandon conveniently its obligations under those same rights." App. 14a (citing 848 F.2d at 995 (other citation omitted)).

Finally, the Federal Circuit declared that it was "just as important" that Shell's apparent breach of its contractual duty to notify SGK of polypropylene produced outside of the license "is itself more likely to frustrate

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[4] App. 12a-13a (citing *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220 (Fed. Cir.) (upholding doctrine of assignor estoppel), *cert. dism'd*, 487 U.S. 1265 (1988); *Foster v. Hallco Mfg. Co.*, 947 F.2d 469 (Fed. Cir. 1991) (*Lear* did not bar enforcement of settlement agreement and consent decree); *Sun Studs, Inc. v. ATA Equip. Leasing, Inc.*, 872 F.2d 978, 991-93 (Fed. Cir. 1989) (*Lear* did not bar enforcement of contract promise to share royalties); *Hemstreet v. Spiegel, Inc.*, 851 F.2d 348, 350-51 (Fed. Cir. 1988) (*Lear* did not bar enforcement of settlement agreement to pay royalties even if patent later held invalid)).

federal patent policy than enforcement of the contract." App. 14a. Describing *Lear* as premised on the "full and free use of ideas in the public domain," *id.* (citing 395 U.S. at 674), the Federal Circuit apparently concluded that Shell should be punished for its silence on grounds that "Shell delayed a timely challenge to the validity of the '698 patent and postponed the public's full and free use of the invention of the '698 patent." App. 14a. The court of appeals did not explain how Shell's failure to invalidate the '698 patent sooner entitles SGK to even more money than it has already received under licenses to an invalid patent.

According to the Federal Circuit, Shell "enjoyed the protection of the license" under the '698 patent from 1987 until SGK learned of the Seadrift process and then, as soon as SGK discovered its existence, Shell "suddenly seeks the protection of the *Lear* policies it flaunted for many years." App. 14a. However, having paid royalties on its old processes for years, Shell flaunted nothing in *Lear* by declining to pay royalties on its new, noninfringeing process, particularly where Shell assumed the risk of having its license terminated for all of its processes, even those for which it had been willing to pay royalties. Moreover, *Lear*'s primary policy was to unmuzzle a licensee to challenge the validity of a licensed patent, and to allow the licensee to avoid paying accrued royalties if it was successful in invalidating the patent. 395 U.S. at 670.

Nevertheless, erroneously assuming that *Lear* reflected a belief by this Court that licensees making successful challenges to a patent's validity should only be excused from paying royalties accruing after notifying the licensor of their validity challenge (an arbitrary deadline and a holding found nowhere in *Lear*), the Federal Circuit announced the following rule:

> [A] licensee, such as Shell, cannot invoke the protection of the *Lear* doctrine until it (i) actually ceases

> payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid.

App. 14a. Without analysis, the Federal Circuit found reassurance by noting that other circuits had arrived at the same conclusion. *See* App. *id.* (and cases cited).

On that basis, the Federal Circuit concluded that enforcing the parties' patent license agreement according to its specific terms would not frustrate federal patent policy—even though that ruling requires the district court and the parties to prolong their four-year litigation to resolve whether Shell's Seadrift process infringes now-invalidated claims of the '698 patent. App. 15a. Now, Shell has filed this timely petition seeking review of the Federal Circuit's incorrect and insupportable rule.

REASONS FOR GRANTING THE WRIT

This petition asks this Court to reject the Federal Circuit's rule of law announced in this case that a patent licensor may still recover damages for breach of contract from its licensee for unpaid royalties after the licensee proves that the licensed patent is invalid by clear and convincing evidence. Absent fraud, once the licensed patent is held invalid, the court should just leave the parties where it found them. Any royalties that have already been paid under the license should stay with the licensor. Conversely, the invalidity of the licensed patent should end any ability of the licensor to recover any additional or past due royalties under any legal theory. No other rule or result makes sense.

When Shell first began using its new Seadrift process, it was confident that the process was not covered by any claim in the '698 patent. By not paying royalties, Shell was exposed to a lawsuit despite having a license under the '698 patent. Had Shell not been a licensee and had SGK sued for patent infringement, Shell would have invalidated

the patent and paid nothing. However, the Federal Circuit has allowed the existence of a license agreement and Shell's alleged failure to notify SGK that its patent was believed to be invalid to provide SGK a legal loophole by which to deny Shell a complete defense of patent invalidity.

By refusing to treat the proven invalidity of a licensed patent as a complete defense to an action for breach of license, the Federal Circuit has authorized using state contract law to accomplish something that federal patent law does not allow: exacting royalties for a known process which is not protected by a valid patent. Blindly following a line of federal court decisions that purport to be upholding a rationale for this Court's decision in *Lear, Inc. v. Adkins,* 395 U.S. 653 (1969), that is nowhere to be found in that decision, the Federal Circuit held that a licensor may continue to litigate to recover royalties that accrued from the time that the licensee ceased paying full royalties until the licensee informed the licensor that the licensed patent was believed to be invalid.

The Federal Circuit's new rule flies in the face of this Court's clear precedent holding that a patentee cannot benefit from an invalid patent and that the public should have full and free use of all ideas in general circulation that are not protected by a valid patent. Yet, prior to making a validity challenge against the licensed patent, a licensee such as Shell has now been estopped by its license because the Federal Circuit has held that proving patent invalidity will not foreclose a contract claim for past royalties under the license. Because the Federal Circuit is not empowered to overrule or disregard *Lear,* this reversion to licensee estoppel is contrary to law and should be reversed by this Court.

Viewed merely as a matter of judicial economy and administration, holding a trial to determine whether an invalid patent has been infringed constitutes a huge and wholly unnecessary waste of public and private resources. As a matter of patent law, such a rule ignores that it is a

complete defense to a charge of infringement to be practicing the prior art, yet the Federal Circuit now has mandated that district courts construe invalid patent claims and decide issues of infringement without regard to the prior art that caused the asserted claims to be held invalid. As a matter of logic, there should be no difference between proving noninfringement and proving invalidity as a full defense to a claim for license royalties.

For the reasons set forth herein, Shell's petition should be granted and the Federal Circuit's decision to allow a patent licensor to recover any unpaid royalties for an invalid patent under a contract theory should be reversed.

I. ALLOWING ROYALTIES UNDER AN INVALID PATENT PURSUANT TO STATE CONTRACT LAW IS PREEMPTED BY FEDERAL PATENT LAW AND IS CONTRARY TO THE PRECEDENT OF THIS COURT

Any idea that is known but not patentable, or that is disclosed in a patent that is later invalidated, cannot be removed from the public domain under the guise of providing some form of alternative protection or remedy under state law. As shown below, repeated decisions from this Court leave no doubt.

In *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225 (1964), and *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964), accused infringers were held to have violated state unfair competition laws by copying the patented device, even though the defendants had proved that the patents were invalid. This Court reversed both judgments, holding that state laws could not be used to frustrate federal patent policy by prohibiting the copying of products or processes not protected by valid patents. *See* 376 U.S. at 230-31.

> Just as a State cannot encroach upon the federal patent laws directly, it cannot, under some other law, such as that forbidding unfair competition, give protection of a kind that clashes with the objectives of the federal patent laws.

Id. at 231-32. Thus, this Court's clear teaching in *Sears* and *Compco* is not limited to state unfair competition laws.

That was confirmed shortly thereafter by *Brulotte v. Thys Co.*, 379 U.S. 29 (1964), which held that licenses requiring royalty payments after the licensed patents had expired were unlawful *per se* as an improper attempt to recover on a patent after the claimed invention has entered the public domain. *Id.* at 32-33. Clearly, a patent license cannot be enforced with respect to any time period in which the licensed patent has no valid or enforceable scope. If *Brulotte* bars using state contract law to allow royalties for an expired patent, the Federal Circuit must have erred by allowing SGK to pursue royalties allegedly due under invalid patent claims that never should have been issued at all.

Most importantly, in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), this Court reiterated its consistent view that federal patent policy outweighs enforcement of state contract law by abrogating the doctrine of licensee estoppel, under which courts had held licensees contractually estopped from using invalidity of the licensed patent as a defense in a suit for royalties due under the license. Recognizing "the strong federal policy favoring free competition in ideas which do not merit patent protection," 395 U.S. at 656, this Court reaffirmed a series of its prior decisions that had already shown that challenges to validity will defeat contractual attempts to insulate patents from attack or to protect a licensor's right to continued royalties.[5]

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[5] *See, e.g., Pope Mfg. Co. v. Gormully*, 144 U.S. 224, 234 (1892) (refusing to grant an injunction to enforce a licensee's promise never to contest the validity of the underlying patent); *Westinghouse Elec. & Mfg. Co. v. Formica Insulation Co.*, 266 U.S. 342 (1924) (allowing assignor to introduce prior art evidence to narrow the scope of the assigned claims); *Scott Paper Co. v. Marcalus Mfg. Co.*, 326 U.S. 249 (1945) (patent assignor could avoid estoppel by showing it had copied an expired patent in the prior art); *Sola Elec. Co. v. Jefferson Elec. Co.*, 317 U.S. 173 (1942) (licensee under

Recognizing a conflict between contract law forbidding a purchaser to repudiate his promises upon becoming dissatisfied with the bargain and federal law requiring that all ideas be dedicated to the common good unless protected by a valid patent, the Court in *Lear* admitted that prior attempts to balance the two competing policies had been a failure. 395 U.S. at 668.

> [Because patents issue from an *ex parte* proceeding], it does not seem to us to be unfair to require a patentee to defend the Patent Office's judgment when his licensee places the question in issue, especially since the licensor's case is buttressed by the presumption of validity which attaches to his patent. Thus, although licensee estoppel may be consistent with the letter of contractual doctrine, we cannot say that it is compelled by the spirit of contract law, which seeks to balance the claims of promisor and promisee in accord with the requirements of good faith.
>
> Surely the equities of the licensor do not weigh very heavily when they are balanced against the important public interest in permitting full and free competition in the use of ideas which are in reality a part of the public domain. . . . We think it plain that the technical requirements of contract doctrine must give way before the demands of the public interest.

Id. at 670. Thus, *Lear* formally authorized licensees to challenge the validity of licensed patents and, if successful, to use such invalidity as a complete defense if the patentee-licensor sues for contract damages.

Any doubt as to the proper meaning of *Lear* should have been eliminated by *Blonder-Tongue Lab., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313 (1971), in which this Court held that any adjudication of patent invalidity estops the patent owner from asserting that same patent against others. In that case, *Lear* was correctly characterized as follows:

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contract with illegal price-fixing clause was allowed to prove invalidity to avoid paying royalties).

> *Lear* permits an accused infringer to accept a license, pay royalties for a time, and cease paying when financially able to litigate validity, secure in the knowledge that invalidity may be urged when the patentee-licensor sues for unpaid royalties.

402 U.S. at 346. Nothing in *Lear* or *Blonder-Tongue* holds that a licensee is required to give notice or take any additional steps that could lead to litigation beyond withholding royalty payments allegedly due under the license.

The facts of *Lear* were somewhat unusual in that Lear had agreed to the license before the patent issued and thus received early disclosure of the secret application. During prosecution, Lear informed Adkins that the claimed idea was not patentable over the prior art, and that the company would pay no further royalties. 395 U.S. at 659. No post-issuance royalties were ever paid. In holding that Lear was not estopped to contest validity, this Court expressly held that "Lear must be permitted to avoid the payment of all royalties accruing after Adkins' 1960 patent issued if Lear can prove patent invalidity." [6] 395 U.S. at 674.

This Court clearly did not envision that any post-issuance royalties could be recovered if the patent in *Lear* was held invalid on remand. Moreover, the Court rejected an attempt to enforce the license provision that royalties were to be paid until such time as the patent was held invalid. 395 U.S. at 673.

> The decisive question is whether the overriding federal policies would be significantly frustrated if licensees could be required to continue to pay royalties during the time they are challenging patent validity in the courts.

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[6] This Court did not decide whether Lear was contractually obligated to pay royalties until the patent issued in exchange for the early disclosure of the pending application. Instead, it remanded that issue to the state court to allow it to "reconcile the competing demands of patent and contract law in a way which would not warrant further review in this Court." 395 U.S. at 675.

> It seems to us that such a requirement would be inconsistent with the aims of federal patent policy. . . . If a licensee has reason to believe that he will replace a patented idea with a new one in the near future, he will have little incentive to initiate lengthy court proceedings, unless he is *freed from liability at least from the time he refuses to pay the contractual royalties.* Lastly, enforcing this contractual provision would undermine the full and free use of ideas in the public domain.

Id. at 673-74 (emphasis added). If an express provision to pay royalties until the patent was declared invalid was not enforced by this Court in *Lear*, the Federal Circuit had no legal basis for allowing an alleged breach of a contract provision merely requiring notice of unlicensed production to justify recovering past due royalties on the invalid claims of the '698 patent.

Because some form of breach will exist whenever a licensee relies on *Lear* to challenge a licensed patent, the mere existence of a breach cannot justify allowing contract law to enable a licensor to seek additional past royalties for a patent that has been held to be invalid. Such a result is clearly preempted by federal patent law and policy as repeatedly announced by this Court. Without question, *Lear* confirms that invalidity of a licensed patent is a complete defense to a contract claim for any royalties that accrued under the license after the licensed patent issued. On its face, the Federal Circuit's contrary rule violates *Lear*, is clearly wrong and should be summarily reversed.

II. THE FEDERAL CIRCUIT VIOLATED *LEAR* BY IGNORING ITS OWN HOLDING THAT THE LICENSED PATENT IS INVALID

As evidenced by the Federal Circuit's admitted efforts to limit or distinguish *Lear* at every opportunity, *see supra* note 4, the Federal Circuit's analysis is this case has again been tainted by its automatic assumption that all patents (even invalid ones) promote the progress of science and

useful arts. *See* U.S. Const., art. I, § 8. To the extent that there is any legitimacy to that court's criticism of *Lear* as reflecting "a past era of skepticism over intellectual property principles," App. 12a, the Federal Circuit is equally susceptible to criticism for its tireless promotion of intellectual property rights in disregard of this Court's precedent.

In this case, the relevant claims of the '698 patent were proven to be invalid, meaning that their existence since 1978 was actually an impediment to progress in science and the useful arts. By failing to give legal effect to its own conclusion that those claims should never have issued, the Federal Circuit has improperly elevated state contract law over federal patent law in a manner that authorizes an undeserving patent owner to pursue even more royalties under a license to an invalid patent. Viewed in that light, as it must be, none of the justifications for that result offered by the Federal Circuit have any merit.

According to the Federal Circuit, contract law governed enforcement of the license because nothing in the parties' agreement made payment of royalties contingent upon the validity of the '698 patent. App. 11a. If the outcome were truly dictated solely by contract law, the invalidity of the licensed patent would not bar a licensor from recovering royalties for the entire patent term anyway. However, even SGK concedes that a licensee can use invalidity as a defense to a licensor's demand for past royalties after the patent is challenged.

In essence, the legal question presented by this petiiton is whether there are *any* circumstances in which invalidity under federal patent law will not trump state contract law in a suit for license royalties. As a matter of constitutional law, the answer can only be "no." Yet inexplicably, the Federal Circuit reached the opposite conclusion, claiming to have been unable to discern a "significant" conflict between state contract and federal patent law in allowing a licensor to recover "pre-challenge" royalties accruing under a license to an invalid patent. App. 13a. For

whatever reason, it is apparent that the Federal Circuit was really not looking very hard.

A. The Federal Circuit's Reasons For Allowing State Contract Law To Override Federal Patent Law Are Baseless

In explaining its rationale for abolishing licensee estoppel, this Court in *Lear* had cited cases criticizing or limiting assignor estoppel as well. *See* 395 U.S. at 663-67. When the Federal Circuit later used its own initiative to resurrect the assignor estoppel doctrine in *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220 (Fed. Cir.), *cert. dism'd*, 487 U.S. 1265 (1988), that court carefully sidestepped *Lear* by drawing a distinction between an assignor and a licensee:

> The public policy favoring allowing a licensee to contest the validity of the patent is not present in the assignment situation. Unlike the licensee, who, without *Lear*, might be forced to continue to pay for a potentially invalid patent, the assignor who would challenge the patent has already been fully paid for the patent rights.

848 F.2d at 1224. In this case, however, the Federal Circuit conveniently ignored that distinction in order to legitimize a contract suit for royalties under a license to an invalid patent in violation of *Lear*. Such conspicuous bootstrapping by a lower court as a means to get around a controlling decision of this Court should not be condoned.

Even if it is assumed that *Diamond Scientific* was factually distinguishable from *Lear*, the Federal Circuit's reliance on *Diamond Scientific*'s rationale as a basis to avoid *Lear* in a license case is wholly improper. Moreover, the Federal Circuit's attempts to equate this case with *Diamond Scientific* are wholly inapt. In contrast to the patent in *Diamond Scientific*, the relevant '698 patent claims have already been litigated, appealed, and held invalid. Nevertheless, the Federal Circuit viewed the two cases as in-

distinguishable because, like the assignor in *Diamond Scientific*, Shell had supposedly also executed a contract "which produced significant benefits for the corporation and attested to the worth of the patent." App. 13a.

It is wrong to assume that a licensee has attested to the worth of the licensed patent or even believes that the patent is valid. A party may take a license to avoid litigation, to preserve business relationships, to minimize uncertainty, or for many other reasons unrelated to the "worth" of the licensed patent. Here, the Federal Circuit did not even try to explain how paying millions for an unnecessary license under an invalid patent "produced a significant benefit" to Shell (rather than an undeserved windfall to SGK). Similarly, the court did not try to reconcile its reliance on the '698 patent's alleged worth with the *de novo* conclusion a few paragraphs earlier that the relevant claims were invalid and thus worthless as a matter of law.

Compounding its analytical errors, the Federal Circuit characterized Shell as having received the "benefits" of producing polypropylene insulated from unlicensed competition, from investigations of infringement, and even from royalties. App. 13a. As confirmed by its own invalidity holding, those alleged "benefits" were either disadvantages or nonexistent. Indeed, the fundamental flaw of the Federal Circuit's legal analysis is that it assumes that the '698 patent is still valid. While that may have been presumed when the license was signed (*see* 35 U.S.C. § 282), it is clear error for the Federal Circuit to perpetuate that overcome presumption to justify a contract claim for post-invalidity royalties.

Far from benefitting from being insulated from unlicensed competition, Shell was clearly disadvantaged by having to compete against those polypropylene companies that never paid any royalties to SGK for the use of processes covered by the '698 patent. As to being free from investigations of infringement, that "benefit" clearly ceased when Shell decided not to pay additional royalties to SGK.

At that point, Shell and its Seadrift process became subject to SGK's investigations, to allegations of breach, and later to the intrusiveness of discovery when SGK terminated the license and filed suit. In fact, litigation did ensue so such freedom from suit was temporary. Because any such freedom from suit attributable to the license only exists while all royalties are being paid, Shell paid in full for whatever benefit it may have received in that regard from its license.

Finally, the Federal Circuit's claim that Shell received a benefit under the license of being free from royalties until SGK discovered the Seadrift process is nonsensical. To the extent that is a benefit at all, it stemmed not from the license, but from Shell's own conclusion that the Seadrift process was outside of the license. Moreover, any such "benefit" was again only temporary because Shell's exposure for the unpaid royalties did not cease upon nonpayment—but should have when Shell established that the relevant claims of the licensed patent were invalid.

By its own admission, the Federal Circuit was acting to prevent the "injustice" of allowing Shell to disclaim the illusory benefits allegedly received under its license by later abrogating the agreement and avoiding all liability for breach. App. 14a. That is not an injustice. The real injustice is allowing SGK to pursue additional royalties under invalid patent claims to subject matter disclosed in the prior art. The greatest injustice is that the Federal Circuit could only reach that result by ignoring *Lear*.

For the period prior to Shell's challenge to the '698 patent, the Federal Circuit has ruled that the proven invalidity of the relevant patent claims has no effect on SGK's cause of action for past royalties under the license. The result for that period is exactly the same as when the doctrine of licensee estoppel still applied. Thus, despite *Lear*, Shell has effectively been estopped by its contract. Whether viewed as a direct violation of this Court's elimination of licensee estoppel in *Lear* or merely as an untenable extension of *Diamond Scientific*'s narrow

rationale beyond any legitimate scope, the Federal Circuit's rule announced in this case should be reviewed and reversed by this Court.

B. Controlling Federal Patent Law Prevents A Contract Remedy Based On Whether Invalid Claims Are Infringed

This Court should not tolerate a rule of law that requires expending additional judicial resources on rewarding a licensor for rights under patent claims that the courts have already held to be invalid. If the Federal Circuit's rule is upheld, the district court and the parties will be required to hold a trial on whether Shell's Seadrift process falls within the scope of claim 1 of the '698 patent, even though the Federal Circuit has agreed that the asserted claim has no valid scope. The whole premise of such an inquiry is too fanciful to be allowed.

In patent cases, infringement and validity issues are undeniably intertwined. *See, e.g., Markman v. Westview Instr., Inc.*, 52 F.3d 967, 976 n.7 (Fed. Cir. 1995) (patent claims must be interpreted the same for validity and infringement), *aff'd*, 116 S.Ct. 1384 (1996). In an infringement trial, Shell would be free to rely on prior art to narrow the scope of the asserted claim. *See, e.g., Westinghouse*, 266 U.S. at 350-51. Yet, in the trial mandated by the Federal Circuit, Shell apparently is foreclosed from relying on the best prior art, *i.e.*, the Belgian Patent, that narrows the claim scope to nothing.

From the outset, SGK has urged interpretations of the '698 patent lacking any support in the claims, the specification, or the prosecution history. Now, the Federal Circuit has affirmed that the asserted claims cannot be interpreted to be valid in light of the prior art. App. 5a-8a. At the same time, the Federal Circuit has essentially freed SGK to continue to urge its claim interpretations unrestricted by the closest prior art because, unlike the usual patent case, SGK no longer has to fear its claims being held invalid. That cannot be the law.

If a patent license can be enforced despite the licensed patent being invalid, there is no principled way to bar enforcement of similar contracts over invalid, fraudulent, or illusory rights. Even confining one's fears to the patent arena, licenses could be enforced by licensors that do not actually own the licensed patent (at least until the licensee challenged ownership). Licenses could be enforced covering patents procured through inequitable conduct or misused by their owners (at least until the licensee challenged the enforceability of the patent). Such results are ridiculous, and illustrate how the Federal Circuit erred in this case in making an exception for invalidity.

While it may be possible to read the words of invalidated claims on another's device or process, for purposes of liability, that is not patent infringement. In that sense, an invalid patent simply cannot be infringed. Moreover, it does not matter why the licensed patent has been invalidated. Whether the licensed patent is invalid as anticipated, obvious, not enabled, or under any other statutory provision, contract law cannot be allowed to supply a basis for liability that is prohibited under the patent law.

C. Invalidity And Noninfringement Should Be Equal Defenses To A Claim For Breach Of A Patent License

Despite rejecting invalidity of the asserted claims as a complete defense to liability for royalties under the '698 patent, the Federal Circuit clearly contemplates that Shell can avoid such liability if the Seadrift process does not infringe claim 1. App. 15a. However, no valid distinction should exist between the effect of proving invalidity or noninfringement as a defense to contract royalties. Indeed, Shell provides a greater public benefit by invalidating the patent claims than by proving only that Shell does not infringe. Yet, if noninfringement is a complete defense to a royalty claim and invalidity is not, licensees will surely focus first on proving the former (with its lower

burden of proof), causing the undesirable result of allowing more invalid patents to remain intact.

In practical effect, the Federal Circuit's ruling penalizes Shell for agreeing to a license, for paying royalties on its older polypropylene processes, and then assuming the risk that additional payments for the new Seadrift process were not needed because that process was not covered by the '698 patent. When SGK terminated Shell's license in 1993, thus exposing Shell's older polypropylene processes to possible infringement liability, Shell maintained its position that the Seadrift process was not covered, but also pursued other available defenses to SGK's suit, ultimately exposing the invalidity of the relevant patent claims.

Regardless of why a patent licensee witholds royalties allegedly owed under a license, invalidity of the licensed patent must be a complete defense to a claim for unpaid royalties. It cannot be the law that it makes a difference in defeating liability under a license whether Shell prevails first on its invalidity defense or its noninfringement defense.

III. OTHER FEDERAL COURTS ERRONEOUSLY PROMOTE AN ILLUSORY POLICY OF EARLY PATENT CHALLENGES THAT IS NOWHERE IN *LEAR*

Admittedly, many post-*Lear* decisions have ruled that a licensee cannot use invalidity as a defense to a claim for past due royalty payments that accrued before the licensee notified the licensor that the licensed patent was believed to be invalid. However, not only is this rule inconsistent with this Court's precedent, but it imposes an arbitrary burden on the licensee that does not even support the illusory policy favoring early challenges to validity on which it is purportedly premised.

The post-*Lear* case most responsible for the creation of this "equitable" rule is *PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700 (6th Cir.), *cert. denied*, 429 U.S. 824 (1976). In that case, the licensee, PPG, ceased

paying royalties because it was dissatisfied with the licensor's efforts to enforce the licensed patent against infringers. At the same time, PPG was actively assisting the licensor in defending the licensed patent's validity in lawsuits with others. *Id.* at 703. When the licensed patent was later invalidated in one of those suits, PPG sought a declaratory judgment that its license agreement was unenforceable, and the patentee counterclaimed for the royalties withheld by PPG prior to filing the declaratory judgment action. *Id.* at 703-04.

Apparently troubled by allowing a licensee that was striving to uphold the validity of the licensed patent to escape liability for its own past due royalties when another party succeeded in invalidating the patent, the Sixth Circuit held that PPG had to pay the past royalties up until the time it brought suit against the licensor. *Id.* at 707. In supporting its result, the Sixth Circuit in *PPG* manufactured a misinterpretation of *Lear* that became a blindly-accepted but clearly erroneous statement of federal patent policy with respect to patent license disputes.

Without citation, the Sixth Circuit declared in *PPG* that "[u]nder *Lear* a licensee has the right to cease paying royalties at any time *for the purpose of prompting an early adjudication of the invalidity of the patent.*" *Id.* at 704 (emphasis added). However, *Lear* stated no such thing. In fact, *Lear* did not even mention the "early adjudication" of patent invalidity as a policy consideration at all. Instead, *Lear* recognized that a licensee "will have little incentive to initiate lengthy court proceedings, unless he is freed from liability at least from the time that he refuses to pay the contractual royalties." 395 U.S. at 673-74.

It is not surprising that promoting early adjudication of patent invalidity was never discussed in *Lear* as being this Court's motivation for eliminating licensee estoppel. In nearly all cases, a licensee (or potential licensee) has an incentive to bring a challenge to a licensed patent as soon as it is aware of grounds to do so because a success-

ful challenge will terminate any obligation to pay royalties or remove any fear of an infringement suit. Thus, by ending licensee estoppel, early adjudication of invalid patents is a natural effect of *Lear*, not its cause.

Simply put, the date upon which the licensor is first notified by the licensee that it believes the patent is invalid is an arbitrary fiction.[7] Upon failing to pay full royalties, a licensee becomes subject to suit by the licensor. If the patent is later shown to be valid and infringed, the licensee will be liable for all royalties due and consequential damages (if the license has not been terminated) or will be liable for infringement damages and other remedies, including an injunction (if the license has been terminated). In light of those significant risks if it loses, the licensee should achieve a complete victory whether the patent is shown to be invalid or not infringed.

Moreover, requiring a licensee to express its belief in invalidity does little, if anything, to initiate court challenges to validity any earlier than they would otherwise arise. Once a licensee withholds any royalties, the specter of litigation arises regardless of whether the licensee also expresses its belief of invalidity as a reason. Moreover, the specific reason for the missing royalties should not matter. If a licensee withholds payments in dispute over the scope of the patent claims, the licensor is just as likely to bring a lawsuit, and in most cases, the validity of the patent will end up being contested as well.

Nevertheless, upon pronouncing early adjudication of invalidity as being *Lear*'s primary objective, the Sixth Circuit in *PPG* then used that policy as a basis for announcing that "something more than mere non-payment is required to encourage an early adjudication of invalid-

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[7] If the Federal Circuit's rule is accepted, licensees will simply inform the licensor that the license is being signed merely to avoid litigation or remove uncertainty even though the licensee believes the patent is invalid. Thus, the rule will likely impede the resolution of license disputes by causing premature litigation, protracted negotiations, and excessive costs with little corresponding benefit.

ity." 530 F.2d at 706 (quotation omitted). At best, the unusual facts in that case led to a holding not generally applicable to all patent licenses or disputes over unpaid royalties. In any event, *PPG* spawned an ill-advised and arbitrary rule neither mandated by this Court in *Lear* nor consistent with the federal policies on which *Lear* was truly based.

IV. THIS PETITION SHOULD BE GRANTED TO CORRECT THE CONFLICT AND CONFUSION CREATED IN THE VARIOUS CIRCUITS SINCE *LEAR*

Despite having different facts than in *PPG*, a number of federal courts in later cases just accepted the Sixth Circuit's proclamation that "early adjudication of patent invalidity" was the primary motivation for *Lear* and assumed—without analysis or question—that the Sixth Circuit's "challenge rule" promoted that policy and accurately interpreted *Lear*. In *American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890, 897 (3d Cir.), *cert. denied*, 449 U.S. 825 (1980), the Third Circuit conceded that *Lear* stated that a licensee's royalty obligation was suspended when royalty payments were halted, yet followed *PPG* anyway. Indeed, *PPG*'s recasting of *Lear* can be found in every federal decision relied on by SGK and cited by the lower courts in this case.[8]

Now, twenty years later, the string of courts citing *PPG*'s error has culminated in the Federal Circuit's misguided decision to adopt that rule as its own precedent in this case. Clearly, the Federal Circuit was concerned that Shell had not informed SGK of the polypropylene made using the Seadrift process until asked. App. 14a. However, any breach in that regard was cured in accordance

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[8] *See* App. 14a-15a & App. 25a (citing *Rite-Nail Packaging Corp. v. Berryfast, Inc.*, 706 F.2d 933, 936-37 (9th Cir. 1983); *Hull v. Brunswick Corp.*, 704 F.2d 1195, 1203-04 (10th Cir. 1983); *Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277, 1283 & n.7 (9th Cir. 1982); *see also Bahamas Paper Co. v. Imperial Packaging Corp.*, 58 F.R.D. 355, 356-57 (S.D.N.Y. 1973); *Eastman Kodak Co. v. GAF Corp.*, 419 N.Y.S.2d 372, 373 (N.Y. Sup. Ct. 1979).

with the license. *See supra* note 3. Moreover, SGK continued to receive royalties from its licensees during the interim, so SGK could hardly have been harmed because Shell did not prove the invalidity of the '698 patent even sooner. Finally, even an uncured breach cannot allow contract law to violate *Lear* and nullify the legal effect of proving a licensed patent to be invalid.

Unlike the Third, Sixth, Ninth, and Tenth Circuits, courts in the Seventh Circuit have upheld the withholding of royalty payments as sufficient to allow proof of invalidity to be a complete defense to contract damages, even in the absence of any prior notice of a challenge to validity. For example, in *Kraly v. Nat'l. Distillers and Chemical Corp.*, 502 F.2d 1366, 1372 (7th Cir. 1974), the court only required royalties to be paid for the period when the licensee was marking its product with the number of the licensed patent, and made no mention of a prior challenge to validity as setting the royalty cut-off date.

A Seventh Circuit district court case, *Crane Co. v. Aeroquip Corp.*, 356 F.Supp. 733 (N.D. Ill. 1973), is factually quite similar to this one. Like Shell, the licensee in *Crane* designed a new device that it believed fell outside the scope of the licensed patent, but continued to pay royalties on its original device. *Id.* at 740. The licensee did not tell the licensor of the new product until the licensor inquired. *Id.* at 735. Rejecting the licensor's attempt to be paid all royalties accruing before its complaint for breach of contract, the court refused to read *Lear* so narrowly as to require actual litigation before a licensee's royalty obligation ceases because such a rule would allow the licensor to wait until the patent expired and then sue for all royalties not paid before the litigation. *Id.* at 740.

In so doing, the district court in *Crane* recognized that invalidity was a complete defense to a claim for unpaid royalties, but reserved decision on whether the licensee would have to pay for the period that it had marked the

new product with the patent number if the patent were held valid. *Id.* at 740-41. Decided before *PPG* and thus not influenced by the Sixth Circuit's error, the court in *Crane* properly cited and relied on *Lear* and *Blonder-Tongue*. Notably, there is no requirement in *Crane* that the licensee must have first informed the licensor that it considered the patent to be invalid.

Because the Federal Circuit is now the federal court of appeals with exclusive jurisdiction over appeals arising under the patent laws, the Federal Circuit's blind adherence to *PPG* and its progeny has now magnified the importance of an already wasteful and erroneous rule of law. To the extent that the Federal Circuit's views on patent-related issues will be given added weight by other federal courts, its serious mistake should be corrected by this Court.[9] Moreover, the importance of resolving the conflicts among the various circuit courts on the important legal question presented by this petition has not been diminished by the existence of the Federal Circuit.

Disputes over patent licenses are not confined only to cases arising under the patent laws.[10] Because of the ever-increasing importance of patents and other intellectual property in the global economy, high-stakes patent license

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[9] This Court has granted certiorari in other cases arising from the Federal Circuit where important federal interests or rules of laws were at issue. *See, e.g., Warner-Jenkinson Co. v. Hilton Davis Chem. Co.*, 117 S. Ct. 1040 (1997) (clarifying judicial-created doctrine of equivalents); *Cardinal Chem. Co. v. Morton Int'l, Inc.*, 508 U.S. 83 (1993) (reviewing Federal Circuit's practice of vacating invalidity holdings upon affirming finding of non-infringement).

[10] *See, e.g., In re Innotron Diagnostics*, 800 F.2d 1077, 1080 n.4 (Fed. Cir. 1986) (Federal Circuit "will not have jurisdiction over an appeal from a district court judgment where the district court's jurisdiction was based solely on diversity, even though the case may involve interpretation, viability, and application of a patent license contract, and those determinations may require consideration of defenses raising patent validity and infringement issues" (and cases cited)).

disputes will continue to confront all federal appellate courts in diversity cases. Thus, wholly apart from the Federal Circuit's adoption of the wrong law as its own precedent, this case presents a perfect opportunity to resolve the confusion between the circuits over the true effect of *Lear* in this situation.

More importantly, the real conflict in this situation is between this Court's precedent in *Lear* and the post-*PPG* decisions of a majority of federal courts, most recently the Federal Circuit, that have disregarded that precedent to redirect federal patent policy as they prefer. Not only are they bound by this Court's precedent, but they have adopted the wrong rule of law. As embodied by *Lear*, the applicable rule in all federal courts should remain that proof of invalidity of a licensed patent ends all liability for unpaid royalties under a license to that patent, and eliminates the need for any further proceedings in the federal courts. Once a licensed patent is held invalid, there should be nothing left to litigate.

CONCLUSION

For each of the above reasons, Shell's petition for writ of certiorari should be granted.

Respectfully submitted,

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September 25, 1997

APPENDIX

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

96-1079

STUDIENGESELLSCHAFT KOHLE, M.B.H.,
Plaintiff-Appellant,

v.

SHELL OIL COMPANY,
Defendant/Cross-Appellant.

Appealed from U.S. District Court
for the Southern District of Texas
Judge Gilmore

DECIDED: May 5, 1997

Before RADER, SCHALL, and BRYSON, *Circuit Judges.*

RADER, *Circuit Judge,*

The United States District Court for the Southern District of Texas determined that claims 1-6 and 14 of U.S. Patent No. 4,125,698 ('698 patent) are invalid, and that infringement of claim 13 by Shell Oil Company's (Shell) polypropylene operations and infringement of claims 7, 9-12, and 15 by Shell's polybutylene operations were not

properly before the court. Studiengesellschaft Kohle m.b.H. (SGK), the owner of the '698 patent, appeals these decisions. Further, the district court certified the following question under 28 U.S.C. § 1292(b) (1994):

> Where the Court has found the relevant patent claims invalid, may the Licensor recover damages for breach of contract for past royalties due on processes allegedly covered by such claims, from the date of the alleged breach until the date that the Licensee first challenged validity of the claims?

Because an applicant cannot combine multiple prior applications to obtain an earlier filing date for an individual claim, this court affirms the district court's invalidity holding. Because infringement involving claim 13 and Shell's polybutylene operations was properly before the district court, this court reverses and remands. Finally, this court answers the certified question in the affirmative.

I.

SGK is the licensing arm of a famous, non-profit research and educational organization in Germany—the Max-Planck Institute for Coal Research. The '698 patent is part of a family of patents filed by Professor Karl Ziegler, a Nobel laureate and past director of the Max-Planck Institute, and various co-inventors. Ziegler and his coworkers initially discovered that combinations of reducing agents (most notably organo-aluminum compounds) and heavy metal compounds would polymerize ethylene to form high molecular plastics. Ziegler extended this discovery to the polymerization of higher members of the ethylene series, such as propylene and butene. Ziegler, et al. filed the 770,484 application, which matured into the '698 patent, on October 29, 1958.

In another case, this court categorized the '698 patent as a continuation-in-part (CIP) because it was not limited to a single parent application. *See Studiengesellschaft*

Kohle m.b.H. v. Northern Petrochemical Co., 784 F.2d 351, 352, 228 USPQ 837, 838 (Fed. Cir. 1986). The 770,484 CIP application, which was filed on October 29, 1958, combined Ziegler's 482,412 application, filed January 17, 1955, with his 514,068 application, filed June 8, 1955. On December 6, 1955, over a year before the filing of the 770,484 application, Belgian Patent No. 538,782 (the Belgian Patent) issued. Claims 1-6 and 14 of the '698 patent, both parties agree, cover a process disclosed in the Belgian Patent.

Shell and SGK first entered into an agreement involving the Ziegler family of patents in 1974. Under that agreement, SGK licensed Shell to polymerize propylene under the Ziegler patents. When the '698 patent issued in 1978, the 1974 agreement already authorized Shell to practice the claimed process. In 1987, after several disputes over this license, Shell and SGK renegotiated the license only with regard to the '698 patent. The new terms provided Shell a paid-up license to produce 450 million pounds of polypropylene per year, with a 1.5% running royalty on any polypropylene sales in excess of 450 million pounds. Further, the amended agreement obligated Shell to give a yearly accounting of its entire polypropylene production. In that yearly accounting, Shell was to "specify the amount of Polypropylene produced which it considers as falling outside of the license and . . . provide SGK, in confidence, with sufficient information to allow SGK to independently evaluate whether or not said production is, in fact, outside of the scope of the license."

In 1987, Shell also began producing polypropylene by an alleged new process in Seadrift, Texas (the Seadrift Process). Because Shell contended that the '698 patent did not cover the Seadrift Process, Shell did not pay royalties on polypropylene produced by that process. Moreover, in its yearly accountings to SGK, Shell did not disclose its production of polypropylene by the Seadrift Process.

Ultimately, SGK terminated Shell's license and brought an action for unpaid royalties from 1987 through 1993. Additionally, SGK set forth claims for infringement of the '698 patent for the period 1993 through 1995. Shell moved for summary judgment of invalidity of claims 1-6 and 14 of the '698 patent based on anticipation by the Belgium patent. SGK responded by arguing that the '698 patent is not anticipated because it is entitled to an earlier filing date than the Belgian patent. To arrive at this earlier filing date, SGK relied on 35 U.S.C. § 120 (1994) to combine the disclosures of the two earlier patent applications (the 482,412 application and the 514,068 application).

The district court held that section 120 does not permit the combination of two earlier disclosures to acquire an earlier filing date, because "an earlier application must comply with the requirements of § 112 for each claim that seeks the benefit of the filing date of that earlier application." As none of the parent applications alone describes the invention recited in claims 1-6 and 14 of the '698 patent, the district court held that these claims were only entitled to the filing date of the continuation-in-part application (October 29, 1958). Thus, the district court determined that the Belgian Patent anticipated claims 1-6 and 14 of the '698 patent, and, therefore, granted summary judgment of invalidity under 35 U.S.C. § 102(b).

The district court further ruled that the only matter remaining before it was SGK's claim for royalties under the parties' license. In that regard, the district court held that a licensor could recover damages for breach of a license agreement where the validity of the underlying patent was not challenged until after the breach occurred. The district court certified the question of whether the invalidity determination on claims 1-6 and 14 would affect plaintiff's claim for unpaid royalties for the period before Shell challenged the validity of the patent.

II.

On appeal, SGK contends that the district court erred in concluding that the disclosures of two earlier filed applications cannot be combined to acquire an earlier filing date under 35 U.S.C. § 120, and in granting summary judgment of invalidity based on that ruling. This court reviews issues of statutory interpretation *de novo*. *See In re Carlson*, 983 F.2d 1032, 1035, 25 USPQ2d 1207, 1209 (Fed. Cir. 1992). Additionally, this court reviews a grant of summary judgment *de novo*. *See Winner Int'l Corp. v. Wolo Mfg. Corp.*, 905 F.2d 375, 376, 15 USPQ2d 1076, 1077 (Fed. Cir. 1990).

Section 120 sets forth the requirements for a patent application to receive the benefit of the earlier filing date from a prior application:

> An application for patent for an invention disclosed in the manner provided by the first paragraph of section 112 of this title in an application previously filed in the United States . . . which is filed by an inventor or inventors named in the previously filed application shall have the same effect, as to such invention, as though filed on the date of the prior application . . . if it contains or is amended to contain a specific reference to the earlier filed application.

35 U.S.C. § 120. To qualify for an earlier filing date, section 120 requires, *inter alia*, that the earlier-filed U.S. patent application contain a disclosure which complies with 35 U.S.C. § 112, ¶ 1 (1994) for each claim in the newly filed application. Thus, this benefit only applies to claims that recite subject matter adequately described in an earlier application, and does not extend to claims with subject matter outside the description in the earlier application. *See Waldermark Link, GmbH & Co. v. Osteonics Corp.*, 32 F.3d 556, 558-59, 31 USPQ2d 1855, 1857 (Fed. Cir. 1994). In other words, a claim complies with 35 U.S.C. § 120 and acquires an earlier filing date if, and

only if, it could have been added to an earlier application without introducing new matter. *See Mendenhall v. Cedarapids, Inc.*, 5 F.3d 1557, 1566, 28 USPQ2d 1081, 1088-89 (Fed. Cir. 1993).

Under 35 U.S.C. § 112, ¶ 1, and consequently under 35 U.S.C. § 120 as well, an applicant must "convey with reasonable clarity to those skilled in the art that, as of the filing date sought, he or she was in possession of the invention." *Vas-Cath Inc. v. Mahurkar*, 935 F.2d 1555, 1563-64, 19 USPQ2d 1111, 1117 (Fed. Cir. 1991). An applicant cannot show possession of an invention based upon a combination of several distinct previous applications unless he shows that one of the applications discloses the invention. *See In re Scheiber*, 199 USPQ 782, 785 (CCPA 1978) (Baldwin, J., concurring). In other words, a claim that relies upon a combination of previously-filed applications is not to be entitled to an earlier filing date because the applicant has not demonstrated possession of the complete invention at the time of an earlier application. *Id.* at 785 ("[A]ppellant is asking [the court] to make the decision that various bits of his claimed invention are supported in the parent applications. . . . The majority opinion properly rejects this approach."). In sum, 35 U.S.C. § 120 requires an applicant to meet the disclosure requirement of § 112, ¶ 1 in a single parent application in order to obtain an earlier filing date for individual claims.

Appellant relies on *Ex Parte Janin*, 209 USPQ 761 (PTO Bd. App. 1980) for the proposition that parent applications may be combined to support a later claim.*

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* SGK additionally relies on *Carusi v. Looker*, 342 F.2d 112, 144 USPQ 670 (CCPA 1965). *Carusi*, however, provides no support for this proposition. First, *Carusi* dealt with conception and reduction to practice in an interference case, rather than 35 U.S.C. § 120. The PTO had previously allowed Looker an earlier effective filing date, but that decision was not challenged on appeal. Second, the prosecution history shows that Looker had successfully added the

In *Janin*, the Board allowed the appellant to rely on the combined disclosure of two parent applications to support a single claim in a later-filed application. The Board distinguished that case from the situation in *Scheiber*: "[H]ere, the basic process and claimed improvement is disclosed in each of the parent applications and it is only in considering the basic starting materials that we have to direct our attention to separate applications to find adequate support." *Janin*, 209 USPQ at 764. *Janin* attempts to distinguish the situation where one patent application discloses most of the claimed invention and the other application only provides one small aspect to complete the claimed invention from a situation where both parent applications contain "various bits and pieces" of the claimed invention. *Id.* The application in *Janin* comes far closer to meeting the § 112, ¶ 1 standard than did the application in *Scheiber*. Nevertheless, Janin's application did not satisfy that standard, despite the Board's allowance of an earlier filing date. The claims at issue in *Janin* were not completely supported by the disclosure of any one parent application, and, thus, could not meet the § 112, ¶ 1 requirement. *Id.* ("[W]e recognize support for the subject matter of claim 13 is dependent upon the combined disclosures of both parent applications."). Accordingly, this court finds unpersuasive the Board's attempt in *Janin* to limit the holding of *Scheiber* and circumvent the § 112, ¶ 1 standard. Thus, this court affirms the district court's ruling that the disclosures of two earlier filed applications cannot be combined to acquire an earlier filing date under 35 U.S.C. § 120.

SGK concedes that it could not add the '698 patent claims to either the 482,412 or the 514,068 applications without introducing new matter. Specifically, the 482,412 application disclosed only the polymerization of ethylene

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claim at issue to one of his parent applications, prior to the filing of his CIP application, without raising a 35 U.S.C. § 112 rejection. Thus, one of the parent applications alone must have contained sufficient disclosure to meet the 35 U.S.C. § 112, ¶ 1 standard.

olefins, while the '698 patent claims polymerization of a broader class of alpha-olefins. Similarly, the 514,068 application disclosed the use of catalysts from a narrower group of metal compounds than the '698 patent. Neither the 482,412 nor the 514,068 application alone shows complete possession of the invention claimed in the '698 patent. Because individual claims of the '698 patent could not have been added to any single, previously-filed application, the '698 patent is not eligible for an earlier filing date. Based on its original filing date, the '698 patent is anticipated by the Belgian Patent.

This court, consequently, affirms the district court's grant of summary judgment of invalidity under 35 U.S.C. § 102(b) of claims 1-6 and 14 of the '698 patent. Additionally, because claims 1-6 and 14 are invalid, this court need not reach the issue of claim construction with regard to these claims.

III.

In its order holding claims 1-6 and 14 invalid, the district court stated:

> The Court ORDERS that Defendant Shell Oil Company's Motion for Summary Judgment That claims 1-6 and 14 of U.S. Patent No. 4,125,698 Are Invalid is GRANTED. Defendant Shell's Motion for Summary Judgment of Noninfringement of U.S. Patent No. 4,125,698 is DENIED as moot. Trial will proceed on Plaintiff Studiengesellschraft Kohle's claim for breach of contract.

The district court declined to rule on infringement of claim 13 by Shell's polypropylene operations and infringement of claims 7, 9-12, and 15 by Shell's polybutylene operations.

Looking first at claim 13, SGK alleges infringement of the '698 patent in its complaint, without specifying any particular claims. The complaint states that SGK "elects to treat defendant's [Shell's] manufacture of polypropylene

as an infringement of plaintiff's [SGK's] U.S. patent 4,125,698." At no point did SGK express an intent to drop its assertion that Shell infringed claim 13. Nevertheless, Shell alleges that SGK implicitly dropped claim 13 from the suit when it failed to reassert that claim after Shell's "dispositive" summary judgment motion.

Shell's sumary judgment motion sought a judgment of noninfringement of claims 1-6 and 14 of the '698 patent. Resolving this motion, the trial court stated: "Defendant's motion for summary judgment is granted. Shell Oil Company has not infringed U.S. Patent No. 4,125,698." SGK, after Shell's motion, reasserted infringement of claims 7, 9-12, and 15 by Shell's polybutylene operations, but did not reassert infringement of claim 13 by Shell's polypropylene operations. SGK, however, did not state that infringement of claims 7, 9-12, and 15 by the polybutylene operations were the only issues remaining in the suit. The record does not reveal, nor does the district court offer, any valid reason for declining to consider the claim 13 infringement question. This court determines that infringement of claim 13 remains before the district court. On remand, the district court will have an opportunity to address this claim.

Next, this court considers the issue of infringement of claims 7, 9-12, and 15 by Shell's polybutylene operations. In its final judgment, the district court perceived "no claim before the Court raising the question of whether any of the defendant's polybutylene operations infringe U.S. Patent 4,125,698." SGK purports to have added infringement by Shell's polybutylene operations to the pleadings by operation of law.

With regard to amendments by operation of law under Fed. R. Civ. P. 15(b), this court applies the law of the regional circuit. *See Biodex Corp. v. Loredan Biomedical, Inc.*, 946 F.2d 850, 856, 20 USPQ2d 1252, 1258 (Fed. Cir. 1991). The Fifth Circuit reviews the denial of a motion to amend pleadings for an abuse of discretion.

See Norman v. Apache Corp., 19 F.3d 1017, 1021 (5th Cir. 1994); *Avatar Exploration, Inc. v. Chevron, U.S.A.*, 933 F.2d 314, 320-21 (5th Cir. 1991). An appellate court, however, may set aside a discretionary decision which rests on an erroneous interpretation of law or on clearly erroneous factual underpinnings. *See A.C. Aukerman Co. v. R.L. Chaides Constr. Co.*, 960 F.2d 1020, 1039, 22 USPQ2d 1321, 1333 (Fed. Cir. 1992) (in banc).

When declining to address infringement of the '698 patent by Shell's polybutylene operations, the district court stated that the claim involving polybutylene appears for the first time in the joint pretrial order. To the contrary, the record reveals that the polybutylene claim first appears in Plaintiff's Memorandum in Opposition to Defendant's Motion for Summary Judgment. In fact, Shell recognized and opposed SGK's introduction of the issue. Thus, the district court clearly erred in finding that SGK only introduced the polybutylene issue at the pretrial order stage.

Further, despite the district court's contrary statement, a plaintiff may—under some circumstances—introduce a new cause of action through its pretrial order. Fed. R. Civ. P. 15(b) permits, with the express or implied consent of the parties, the trial of issues not raised by the pleadings. Although this court is unaware of any Fifth Circuit Court of Appeals case law directly addressing introduction of a new cause of action through a pretrial order, *but see Marsh Inv. Corp. v. Langford*, 620 F. Supp. 880, 883 (E.D. La. 1985); *Silver v. Nelson*, 610 F.Supp. 505, 520 (E.D. La. 1985), the Fifth Circuit has advocated a liberal policy toward allowing such amendments, *see Mineral Indus. & Heavy Const. Group v. Occupational Safety and Health Review Comm'n*, 639 F.2d 1289, 1292 (5th Cir. 1981). Additionally, other circuits have permitted introduction of new causes of action through both stipulations and pretrial orders. *See Blackwell v. Regal Cab Co.*, 316 F.2d 398, 399-400 (D.C. Cir. 1963); *Bucky v. Sebo*, 208 F.2d 304, 305 (2d Cir. 1953); *see*

also 3 James Wm. Moore, *Moore's Federal Practice*, ¶ 15.13[2] (2d ed. 1996). Because the district court erred in overlooking the Fed. R. Civ. P. 15(b) procedure, and clearly erred in finding that SGK delayed raising infringement by Shell's polybutylene operations until the pretrial order, this court reverses, and remands the issue of infringement of claims 7, 9-12, and 15 for further consideration.

IV.

The district court also certified a question concerning the effect of an invalidity finding on unpaid royalties. *See* 28 U.S.C. § 1292(b) (1994). According to the 1987 licensing agreement, Shell agreed to pay SGK a 1.5% running royalty on the sale of any polypropylene, produced with a heavy metal catalyst as defined in claim 1 of the '698 patent, in excess of 450 million pounds per year. Further, as discussed above, this agreement obligated Shell to give a yearly accounting of its entire polypropylene production, specifying "the amount of Polypropylene produced which it considers as falling outside of the license." The agreement obligated Shell to provide SGK with sufficient information to allow independent evaluation of whether its production falls outside the scope of the license. The record shows that Shell breached this contract by producing polypropylene under the Seadrift Process, without either paying royalties or reporting the production as outside of the license.

Nothing in this license made payment of royalties contingent upon the validity of the '698 patent. Setting aside momentarily both federal patent law and policy, this contract—regardless of the patent's validity—obligates Shell to pay royalties on polypropylene produced in accordance with claim 1 of the '698 patent. In other words, contract law governs the enforcement of the license. Enforcement of these contract terms is not contingent upon validity of the patent which defines the subject matter of the license. Assuming that the Seadrift Process infringes claim 1 of the

'698 patent and thus fits within the terms of the license, Shell breached the license by failing to pay royalties. Enforcement of the license, if the Seadrift Process infringes the '698 patent, would require Shell to pay back royalties.

With a patent licensing agreement at stake, this court examines the contract for rare, but potential, conflicts between state contract law and federal patent law. For example, in *Lear v. Adkins*, 395 U.S. 653 (1969), the Supreme Court prevented the enforcement of a valid royalty payment agreement to facilitate a determination of patent validity. Specifically, the Supreme Court declined to estop a patent licensee from contesting the validity of the licensed patent. *See id.* at 674; *Cordis Corp. v. Medtronic, Inc.*, 780 F.2d 991, 995, 228 USPQ 189, 191-92 (Fed. Cir. 1985). In tones that echo from a past era of skepticism over intellectual property principles, the Court in *Lear* feared that

> [l]icensees may often be the only individuals with enough economic incentive to challenge the patentability of an inventor's discovery. If they are muzzled, the public may continually be required to pay tribute to would-be monopolists without need or justification. We think it plain that the technical requirements of contract doctrine must give way before the demands of the public interest . . . .

Lear, 395 U.S. at 670. Thus, in examining the interface between national patent policy and state contracts, the Supreme Court requires this court to consider "whether overriding federal policies would be significantly frustrated" by enforcing the license. *Id.*

This court encountered the *Lear* test when an assignor-inventor and his company sought to defend against an infringement action by challenging the validity of the assigned patents. *See Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220, 6 USPQ2d 2028 (Fed. Cir. 1988). With careful consideration of the *Lear* test and policies,

this court nonetheless estopped the assignor from challenging the validity of the patent:

> To allow the assignor to make that representation [of the worth of the patent] at the time of the assignment (to his advantage) and later to repudiate it (again to his advantage) could work an injustice against the assignee. . . . [D]espite the public policy encouraging people to challenge potentially invalid patents, there are still circumstances in which the equities of the contractual relationships between the parties should deprive one party . . . of the right to bring that challenge.

Diamond Scientific, 848 F.2d at 1224-25. Indeed, in several other settings, this court has distinguished *Lear. See, e.g., Foster v. Hallco Mfg. Co.,* 947 F.2d 469, 476-77, 20 USPQ2d 1241, 1246-47 (Fed. Cir. 1991) (*Lear* does not bar enforcement of settlement agreement and consent decree); *Sun Studs, Inc. v. ATA Equip. Leasing, Inc.,* 872 F.2d 978, 991-93, 10 USPQ2d 1338, 1349-41 (Fed. Cir. 1989) (*Lear* does not bar enforcement of contract promise to share royalties); *Hemstreet v. Spiegel, Inc.,* 851 F.2d 348, 350-51, 7 USPQ2d 1502, 1504 (Fed. Cir. 1988) (*Lear* does not bar enforcement of settlement agreement to pay royalties even if patent later held invalid).

As in *Diamond Scientific,* this court detects no significant frustration of federal patent policy by enforcing the 1987 license agreement between Shell and SGK, to the extent of allowing SGK to recover royalties until the date Shell first challenged the validity of the claims. First, as in *Diamond Scientific,* Shell executed a contractual agreement which produced significant benefits for the corporation and attested to the worth of the patent. Under the agreement (with its provision for Shell to notify SGK of all polypropylene production), Shell had the benefits of producing polypropylene insulated from unlicensed competition, insulated from investigations of infringement, and even insulated from royalties (until SGK's discovery of the

Seadrift Process). To these benefits, Shell now seeks to add the benefit of abrogating its agreement and avoiding its breach of the contract. Following the reasoning of *Diamond Scientific,* this court must prevent the injustice of allowing Shell to exploit the protection of the contract and patent rights and then later to abandon conveniently its obligations under those same rights. *See Diamond Scientific,* 848 F.2d at 1224-25; *see also Cordis Corp.,* 780 F.2d at 995 (quoting *Warner-Jenkinson Co. v. Allied Chem. Corp.,* 567 F.2d 184, 188, 193 USPQ 753, 757 (2d Cir. 1977) ("It would not be fair for the [licensee] to be allowed simultaneously to reap all the benefits of the licensing agreement and to deprive the licensor of all his royalties.")).

Just as important, however, Shell's apparent breach of its duty to notify under the agreement is itself more likely to frustrate federal patent policy than enforcement of the contract. As already noted, *Lear* focused on the "full and free use of ideas in the public domain." *Lear,* 395 U.S. at 674. By abrogating its notification duty, Shell delayed a timely challenge to the validity of the '698 patent and postponed the public's full and free use of the invention of the '698 patent. Shell enjoyed the protection of the license from 1987 until SGK became aware of the Seadrift Process. Upon SGK's discovery of its Seadrift process, Shell suddenly seeks the protection of the *Lear* policies it flaunted for many years. However, a licensee, such as Shell, cannot invoke the protection of the *Lear* doctrine until it (i) actually ceases payment of royalties, and (ii) provides notice to the licensor that the reason for ceasing payment of royalties is because it has deemed the relevant claims to be invalid. Other circuits addressing this issue have arrived at the same conclusion. *See, e.g., Rite-Nail Packaging Corp. v. Berryfast, Inc.,* 706 F.2d 933, 936-37 (9th Cir. 1983); *Hull v. Brunswick Corp.,* 704 F.2d 1195, 1203 (10th Cir. 1983); *American Sterilizer Co. v. Sybron Corp.,* 614 F.2d 890, 897-98 (3d Cir. 1980);

PPG Indus., Inc. v. Westwood Chem., Inc., 530 F.2d 700, 706, 708 (6th Cir. 1976).

In this factual setting, therefore, enforcement of the license according to its terms, even if this entails a determination of whether the Seadrift process infringes a now-invalidated patent, does not frustrate federal patent policy. Accordingly, this court remands this case to the district court for enforcement of the license (prior to the date Shell first challenged the validity of the claims) and, if necessary, computation of back royalties.

V.

In accordance with this opinion, this court affirms the district court holding that claims 1-6 and 14 are invalid under 35 U.S.C. § 102(b). This court, however, remands the case to the district court for proper consideration of infringement of claim 13, infringement by Shell's polybutylene operations, and infringement of the '698 patent by the Seadrift Process—including a determination of back royalties if necessary.

COSTS

Each party shall bear its own costs.

AFFIRMED-IN-PART, REVERSED-IN-PART, AND REMANDED

[Entered Aug. 31, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

Civil Action No. H-93-3267

STUDIENGESELLSCHAFT KOHLE, M.B.H.,
Plaintiff,

VS.

SHELL OIL COMPANY,
Defendant.

ORDER

On this day the Court considered two motions for summary judgment filed by the defendant (Instrument Nos. 36 and 39). Having reviewed the submissions of both parties and the relevant law, the Court concludes that no triable issues of fact exist regarding the validity of the claims presented in U.S. Patent No. 4,125,698 (the "'698 patent") (Def.'s Ex. A.) The motion for summary judgment on the validity of claims 1-6 and 14 of the '698 patent is granted and the breach of contract cause of action is dismissed as a matter of law. The motion for summary judgment on the infringement cause of action is moot as a matter of law.

I.

The above-referenced case is an action for breach of contract and patent infringement arising from the manufacture of polypropylene. Studiengesellschaft Kohle, m.b.H. ("SGK") is a German corporation that holds rights to a number of patents including the '698 patent. Shell

is a Delaware corporation having its principal place of business in Houston. Shell has a plant in Seadrift, Texas that manufactures propylene polymers.

At issue is whether Shell's Seadrift plant manufactured polypropylene using a method set forth in a valid patent. The '698 patent describes the polymerization of alpha-olefins such as propylene with the use of a catalyst. The application for the patent, Application Serial No. 770,484 (the "'698 application") was filed on October 29, 1958. The patent was issued on November 14, 1978. The '698 patent is related to a number of earlier filed applications: (1) Serial No. 469,069 ("Z1") was filed on November 15, 1954; (2) Serial No. 482,412 ("Z2") (Def.'s Ex. F) was filed on January 17, 1955; (3) Serial No. 514,068 ("Z4") (Def.'s Ex. H) was filed on June 8, 1955; and Serial No. 527,413 ("Z5") (Def.'s Ex. I) was filed on August 9, 1955. The '698 patent and all of the related applications were filed by the same individuals and each relates to the polymerization of olefins using a catalyst. The catalyst in each application consists of two components, one organo-aluminum compound and one heavy metal compound.

SKG claims that Shell (1) failed to pay royalties from the sale of excess polypropylene pursuant to a license agreement between the parties, (Compl., ¶ 4, 5), and (2) infringed a patent held by SGK by using one or more of its patented processes to manufacture polypropylene, (*id.* at ¶ 9).[1] In the alternative, SKG seeks a declaratory judgment on the issue of infringement. (*Id.* at 5.)

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[1] In the pretrial order, SGK claims that Shell infringed the '698 patent by producing polybutylene. This claim does not appear in the complaint, nor did SGK request leave to file an amended complaint to add such a complaint. Rather, the claim for infringement by producing polybutylene appears for the first time in the joint pretrial order. This second infringement claim is separate from the infringement claim included in the complaint. This claim is not properly before the Court. The plaintiff may not bring new and separate causes of action through its pretrial order. The claim for

II.

Summary judgment is proper when pleadings and evidence on file, along with affidavits, show that there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c). The substantive law determines which facts are material, *Anderson v. Liberty Lobby, Inc.*, 106 S.Ct. 2505, 2509-10 (1986), and the court must view these facts and the inferences to be drawn from them in the light most favorable to the party opposing the motion. *Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp.*, 106 S.Ct. 1348, 1356 (1986) (citing *United States v. Diebold, Inc.*, 82 S.Ct. 993, 994 (1962)); *Reid v. State Farm Mut. Auto. Ins. Co.*, 784 F.2d 577, 578 (5th Cir. 1986).

The burden of proof is on the moving party to show an absence of evidence to support the nonmoving party's case. *Celotex Corp. v. Catrett*, 106 S.Ct. 2548, 2552-55 (1986). Once this burden has been met, the nonmoving party can resist the motion for summary judgment by making a positive showing that a genuine dispute of material fact does indeed exist and that it consists of more than bare allegations in briefs and pleadings. *Anderson*, 106 S.Ct. at 2511.

Summary judgment is appropriate in a patent case as in any other where no genuine issue of material fact is present and the movant is entitled to judgment as a matter of law. *Jonsson v. Stanley Works*, 903 F.2d 812, 816 (Fed. Cir. 1990); *Haynes Int'l, Inc. v. Jessop Steel Co.*, 8 F.3d 1573 (Fed. Cir. 1993), *clarified on reh'g in part*, 15 F.3d 1076 (Fed. Cir. 1994). In order to defeat summary judgment, the non-movant's evidence must present a question of material fact which requires submission to a jury. *Jonsson*, 903 F.2d at 816.

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infringement through the production of polybutylene does not exist as a triable claim in this action and cannot be considered.

III.

Shell requests summary judgment that claims 1-6 and 14 of the '698 patent are not valid. The defendant bears the burden of establishing facts by clear and convincing evidence that would require a conclusion of invalidity of the patent. 35 U.S.C. § 282; *American Hoist & Derrick Co. v. Sowa & Sons,* 725 F.2d 1350 (Fed. Cir.), *cert. denied,* 105 S.Ct. 95 (1984). A patent is presumed valid. 35 U.S.C. § 282.

At the outset, the Court holds that the '698 application is a "continuation-in-part," or CIP application. SGK maintains that the application is instead a "continuation," relying on the language of the cover page of the patent. The evidence does not support this conclusion. The Patent Examiner and the Federal Circuit have held that the '698 application was a continuation in part and this Court is persuaded by the reasoning of each. (*See* Def.'s Ex. J at 3.) *See also Studiengesellschaft Kohle, m.b.H. v. Northern Petrochemical Co.,* 784 F.2d 351, 352 (Fed. Cir.), *cert. dismissed,* 106 S.Ct. 3343 (1986).

Shell argues that claims 1-6 and 14 are invalid because the claims are anticipated by Belgian Patent No. 538,782 ("the Belgian patent") (Def.'s Ex. B). Section 102(b) of Title 35 of the United States Code states that a person shall be entitled to a patent unless "the invention was patented or described in a printed publication in this or a foreign country or in public use or on sale in this country, more than one year prior to the date of the application for patent in the United States." If a prior art reference discloses each and every limitation set forth in a claim, then that claim is "anticipated" by the prior reference. *Orthokinetics, Inc. v. Safety Travel Chairs, Inc.,* 806 F.2d 1565, 1574 (Fed. Cir. 1986). In order to determine whether each claim of a patent is invalid under § 102(b), the court must determine the effective filing date of each claim. The '698 application must have been filed within one year of

the patent date of the prior art reference before the patent claims may be found valid.

Shell maintains that the effective filing date of the '698 patent can be no earlier than the date that the '698 application was actually filed, which falls outside the one-year period. SGK appeals to 35 U.S.C. § 120. Under 35 U.S.C. § 120, a patent applicant may receive the benefit of an earlier filing date based on earlier U.S. patent applications.[2] Claims containing matter introduced in the parent application are entitled to the filing date of the parent application, but claims with matter introduced in the CIP are accorded the filing date of the CIP application. *Waldemar Link v. Osteonics Corp.*, 32 F.3d 556, 558 (Fed. Cir. 1994). The benefit of an earlier filing date is limited to those claims that recite subject matter described in an earlier application, and does not extend to any claims that may recite subject matter not properly described in an earlier application. *Id.* "A patentee cannot obtain the benefit of the filing date of an earlier application where the claims in issue could not have been made in the earlier application." *Mendenhall v. Cedarapids, Inc.*, 5 F.3d 1557, 1566 (Fed. Cir. 1993), *cert. denied*, 114 S.Ct. 1540 (1994). In order for a claim of the '698 patent to receive the benefit of a filing date prior to October 29, 1958, the invention recited in that claim must be described in either Z2, Z4, or Z5 in the manner provided by the first paragraph of 35 U.S.C. § 112.

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[2] An application for patent for an invention disclosed in the manner provided by the first paragraph of [35 U.S.C. § 112] in an application previously filed in the United States, or as provided by section 363 of this title, by the same inventor shall have the same effect, as to such invention, as though filed on the date of the prior application, if filed before the patenting or abandonment of or termination of proceedings on the first application or on an application similarly entitled to the benefit of the filing date of the first application and if it contains or is amended to contain a specific reference to the earlier filed application.

Id.

As mentioned, the court must determine whether the previous claims contained sufficient disclosure under 35 U.S.C. § 112, first paragraph.[3] *Waldemar,* 32 F.3d at 558, *citing Utter v. Hiraga,* 845 F.2d 993, 998 (Fed. Cir. 1988). This is a question of law. *Id.* However, compliance with the written description aspect of § 112 is a question of fact. *Id.*

Summary judgment is inappropriate where the resolution of what the parent disclosure conveyed to those skilled in the art presents a material issue of fact. *Vas-Cath Inc. v. Mahurkar,* 935 F.2d 1555, 1567 (Fed. Cir. 1991). The fact finder must determine whether one skilled in the art, reading the original specification, would immediately discern the limitation at issue in the parent. *Waldemar,* 32 F.3d at 558, *citing In re Rasmussen,* 650 F.2d 1212, 1215 (C.C.P.A. 1981). A specification might enable one of skill in the art to practice an invention, without actually providing a written description of that invention. *Vas-Cath,* 935 F.2d at 1561. If there is a genuine dispute as to this issue then summary judgment is not proper. The circumstances surrounding the prosecution of the patent application are also relevant. *Waldemar,* 32 F.2d at 559.

The parties disagree as to the way in which the Court should determine whether the requirements of § 112 were met by previous claims. This is a dispute of law, not fact. SGK argues that the Court should compare each claim in the '698 patent to all of the contents of the parent applications taken together. This argument is unsupported by statutory and case law. The language of § 120 does not support the contention that the later application should be

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[3] 35 U.S.C. § 112, first paragraph states:

> The specification shall contain a written description of the invention, and of the manner and process of making and using it, in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains, or with which it is most nearly connected, to make and use the same, and shall set forth the best mode contemplated by the inventor of carrying out his invention.

compared against a composite of all other related applications. The statute strongly implies that the later application shall be measured against each single parent application taken separately. An earlier application must comply with the requirements of § 112 for each claim that seeks the benefit of the filing date of that earlier application. Consequently, the Court should reject SGK's interpretation of the legal standard relevant to this case.

Neither Z2, Z4, nor Z5 describes the invention recited in claims 1-6 and 14 of the '698 patent.[4] Each is discussed in turn.

The Z2 application is limited to the polymerization of ethylene and does not mention the polymerization of other olefins, while claims 1-6 and 14 of the '698 patent are directed to the polymerization of all alpha-olefins. (Def.'s Ex. F, at 1-2; Decl. of Robert Grubbs, Def.'s Ex. G, ¶¶ 8, 10.) SGK counters that page 7 of the Z2 application includes a paragraph relating to the polymerization of other olefins, but presents no evidence to create an issue of fact as to whether one skilled in the art could construe the specification as describing a process for the polymerization of olefins other than ethylene. (*See id.*, ¶ 10). Moreover, the Fifth Circuit has essentially rejected SGK's interpretation of that paragraph. *See, e.g., Studiengesellschaft Kohle, m.b.H. v. Eastman Kodak Co.*, 616 F.2d 1315, 1334-35 (5th Cir. 1980).

The Z2 application also does not describe the catalyst in the '698 patent claims because the former discloses the use of compounds of Group VIII metals or compounds of manganese only if the aluminum compound is a dialkyl or diaryl aluminum monohalide. (Def.'s Ex. F, at 2, 6.) Claims 1-6 and 14 of the '698 patent are much broader, because they recite using Group VIII metals or manganese with a wide variety of aluminum compounds. SGK does not dispute this deficiency in the Z2 disclosure. Instead, SGK attempts to import from the '698 specification the

[4] The Z1 application is not relevant to this discussion.

limitation that compounds of Group VIII metals or manganese are only to be used with the dialkyl or diaryl aluminum monohalides.

However, "while it is true that the claims should be interpreted *in light of* the specification and with a view to ascertaining the invention, it does not follow that limitations from the specification may be read into the claims. . . . ." *Sjolund v. Musland,* 847 F.2d 1573, 1581 (Fed. Cir. 1988) (emphasis in original). The catalyst used in claims 1-6 and 14 of the '698 patent is broader in scope than the catalyst described in the Z2 application. Thus, Z2 does not describe the catalyst recited in claims 1-6 and 14 of the '698 patent.

The Z4 application differs from the '698 patent in that the former excludes the use of heavy metal oxides in the polymerization catalyst. (Def.'s Ex. H, at 5.) The '698 patent cites a heavy metal component of the catalyst that includes freshly precipitated oxides of particular metals. (Ex. A, cols. 21-22; Ex. G, ¶ 14.) SGK says the Z4 specification describes the use of heavy metal oxides to polymerize olefins. However, the Court concludes that this fact dispute is not genuine. The Z4 application does not contain a written description of heavy metal oxides as a component of the claimed catalyst. Nor does Z4 describe polymerization using Group VIII heavy metals or manganese; SGK does not dispute this. (Def. App. A31.)

In addition, Z4 does not discuss a polymerization process carried out at a pressure between atmospheric pressure and 100 atmospheres. Claim 5 of the '698 patent does. The Z4 application does not describe a polymerization process carried out at a pressure above 25 atmospheres.

It is undisputed that Z5 (1) does not describe a process for polymerizing olefins having more than two carbon atoms and (2) does not mention Group VIII metals or manganese.

SGK contends incorrectly that the Belgian patent is not prior art by virtue of its publication date. Shell provides

ample and sufficient factual evidence to establish that the Belgian patent is effective as a prior art patent as of the date the patent was issued, December 6, 1955. (*See* Def.'s Exs. B at 1; M, Manual of Patent Examining Procedures § 901.05(F)(3)(5th Ed. Rev. 1994).) That the patent was not published until July 3, 1959 is of no relevance.

It is undisputed that Example 22 of the Belgian patent describes a process that satisfies every limitation of claims 1-6 and 14 of the '698 patent. (Def.'s App. A20; Def.'s Ex. C, at 41-42). If the experiment described in Example 22 of the Belgian patent were conducted today, the experiment would infringe each of claims 1-6 and 14 of the '698 patent. Example 22 of the Belgian patent anticipates these claims. *Polaroid Corp. v. Eastman Kodak Co.*, 789 F.2d 1556, 1573 (Fed. Cir.), *cert. denied*, 107 S.Ct. 178 (1986). Example 22 only discloses one species recited in the '698 patent claims. That is enough because a reference disclosing a species anticipates claims to the genus. *Titanium Metals Corp. of America v. Banner*, 778 F.2d 775, 782 (Fed. Cir. 1985).

The '698 patent is not entitled to the benefit of an earlier filing date under 35 U.S.C. § 120. All of the claims included in the '698 patent but not described in the parent applications as discussed above must take the filing date of the continuation-in-part application, October 29, 1958.

The Belgian patent was available as a reference long before the '698 patent was filed. Any claims of the '698 patent which are not entitled to an earlier filing date are invalid under 35 U.S.C. § 102(b). The claims of the '698 patent which are the subject of SGK's breach of contract cause of action all relate to the manufacture of polypropylene and, as those claims are invalid, the breach of contract cause of action must be dismissed. The remaining claim for patent infringement is moot insofar as that cause of action is based on the claims held invalid by this Order.

Throughout its responsive pleadings and the hearing on this motion, SGK argues that its claim for breach of contract remains viable even if this Court holds that the patent forming the basis for the licensing agreement is invalid. SGK claims that Shell breached the license agreement by underreporting its production and sale of polypropylene and underpaying royalties on such production. SGK wishes to recover the amount owed in royalties and other damages it claims to have suffered as the result of such breach.

It is not clear whether SGK is entitled to recover royalty payments or damages for breach of contract arising from a license agreement based on a patent which is ultimately held to be invalid. Several circuits have held that equity requires that the licensor recover royalties incurred before and until the validity of the underlying patent is challenged. *Compare Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277 (9th Cir. 1982) (allowing recovery of royalties accrued but not paid before date licensee challenged validity) *with PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700 (6th Cir.) (affirming award of back royalties from date of cessation of payments until filing date of lawsuit despite invalidity of underlying patent), *cert. denied*, 97 S.Ct. 76 (1976) *and American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890 (3d Cir.) (allowing royalty payment until validity of patent challenged by filing lawsuit), *cert. denied*, 101 S.Ct. 88 (1980). The Federal Circuit has not addressed the issue of back royalties directly. However, the Federal Circuit determined that the law does not require that a licensor recover damages for breach of a license agreement based on an invalid patent where the licensee has not sued for royalties. *RCA Corp. v. Data Gen'l Corp.*, 887 F.2d 1056 (Fed. Cir. 1989). Whether claims for breach of contract survive depends in part on the facts presented in each case. *Id.* This Court concludes that current law on this issue does not prohibit the licensor from recovering damages sustained from the breach of a licensing agree-

ment where the validity of the underlying patent was not challenged until after the breach allegedly occurred.

This issue may not be resolved on summary judgment. Among other things, the parties dispute whether Shell underreported its sales and production of polypropylene under the licensing agreement. Shell answers the breach of contract claim by asserting that it paid royalties on all of its production and sale of polypropylene that was covered by the '698 patent. Consequently, Shell argues, it did not breach the license agreement.

The Court concludes that this dispute is factual and genuine. Summary judgment is precluded on the breach of contract claim and parties will proceed to trial on this issue.

IV.

The Court ORDERS that Defendant Shell Oil Company's Motion for Summary Judgment That Claims 1-6 and 14 of U.S. Patent No. 4,125,698 Are Invalid is GRANTED. Defendant Shell's Motion for Summary Judgment of Noninfringement of U.S. Patent No. 4,125,698 is DENIED as moot. Trial will proceed on Plaintiff Studiengesellschaft Kohle's claim for breach of contract.

The law affords the movant an opportunity to file motions to reconsider and the like pursuant to Fed. R. Civ. P. 59 or 60; however this Court reserves the right to sua sponte impose Rule 11 SANCTIONS, for the wasteful and frivolous re-urging of evidence or legal authority that has already been presented to the Court. A motion seeking relief from or reconsideration of this Order will be granted only in rare circumstances. The parties are instructed to seek whatever relief they desire in the United States Court of Appeals for the Fifth Circuit. If a party seeks reconsideration on the basis of evidence that was available before the issuance of this order but that was not submitted in a timely fashion, the movant must show either excus-

able neglect or manifest injustice for failure to provide these materials to the Court earlier.

SIGNED this 31st day of August, 1995.

/s/ Vanessa D. Gilmore
VANESSA D. GILMORE
United States District Judge

[Entered Sep. 29, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

Civil Action No. H-93-3267

STUDIENGELSELLSCHAFT KOHLE, M.B.H.,
Plaintiff,

versus

SHELL OIL COMPANY,
Defendant.

ORDER

Pending before the Court is the motion of the Defendant for Reconsideration of the Court's Order of August 31, 1995 (Instrument #80) and the motion of the Plaintiff for Entry of a Final Judgment to allow an interlocutory appeal (Instrument #81). It is clear from the respective motions and responses of the parties that some clarification of the Court's August 31, 1995 is warranted and that an interlocutory appeal in this matter would be appropriate.

Defendant points out that the introductory paragraph of the Court's order states that the breach of contract issue is dismissed as a matter of law. That conclusion is based on the Court's finding that the claims of the '698 patent which are the subject of SGK's breach of contract cause of action all relate to the manufacture of polypropylene, which claims have been determined to be invalid by the Court's order (See Court Order at p. 10). The finding of invalidity also makes it unnecessary for the Court to

rule on the merits of the Defendant's motion for summary judgment of noninfringement. The confusion arises because as the Defendant also notes, the Court's order goes on to say that the trial will proceed on the breach of contract claim. Some clarification on this point is in order.

Throughout its responsive pleadings and the hearing on this motion, SGK argued that its claim for breach of contract would remain viable even if this Court held that the patent forming the basis for the licensing agreement is invalid. The Court noted that several circuits have held that equity requires that the licensor recover royalties incurred before and until the validity of the underlying patent is challenged. *Compare Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277 (9th Cir. 1982) (allowing recovery of royalties accrued but not paid before date licensee challenged validity) *with PPG Indus., Inc. v. Westwood Chem., Inc.*, 530 F.2d 700 (6th Cir.) (affirming award of back royalties from date of cessation of payments until filing date of lawsuit despite invalidity of underlying patent), *cert. denied*, 97 S.Ct. 76 (1976) *and American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890 (3d Cir.) (allowing royalty payment until validity of patent challenged by filing lawsuit), *cert. denied*, 101 S.Ct. 88 (1980). Although the Court found that the Federal Circuit has not addressed the issue of back royalties directly, the Court concluded that current law on this issue would not prohibit the Plaintiff from recovering damages for back royalties from the date of the alleged breach until the date that the Defendant challenged the validity of the claims.

Accordingly, as there were fact issues in dispute about whether Shell had breached the contract prior to the time that it challenged the validity of the patent claims, summary judgment on that portion of the Plaintiff's breach of contract claim *relating to back royalties only* was denied. Therefore, contrary to the assertions in Shell's motion, trial of the SGK's breach of contract claim will not depend on the same issues raised in the infringement claim. In-

deed, the issue of infringement or validity will not be an issue at all. The sole issue for the Court to determine will be whether Shell breached the contract by failing to pay all royalties that were owed on its production and sale of polypropylene up to the date that it challenged the validity of the patent.

Both parties have suggested that the Court consider entering an order allowing an interlocutory appeal. Shell argues that the issue of whether SGK is entitled to seek past royalties for processes covered by the invalid claims is a question that would be appropriate for interlocutory appeal and SGK argues that the issue of patent validity would be appropriate for interlocutory appeal. The Court agrees that interlocutory appeal would be appropriate under 28 U.S.C. § 1292(b), but only on the issue of whether SGK is entitled to seek past royalties for processes covered by the invalid claims. Accordingly,

Shell's Motion for Reconsideration (Instrument #80) is DENIED. Plaintiff's Motion for Entry of Final Judgment (Instrument #81) is also DENIED.

IT IS FURTHER ORDERED that the parties may pursue an interlocutory appeal pursuant to 28 U.S.C. § 1292(b) solely on the issue of whether Plaintiff may recover damages for breach of contract for royalties owed from the date of the alleged breach until the date that the Defendant challenged the validity of the claims. The proceedings in this case will be stayed pending the appeal. The file will be administratively closed and the parties are ORDERED to move for a lifting of the stay within ten days from the date that the appeal is concluded.

Signed this 28th day of September, 1995.

/s/ Vanessa D. Gilmore
VANESSA D. GILMORE
United States District Judge

[Entered Oct. 11, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

Civil Action No. H-93-3267
Judge Vanessa D. Gilmore

STUDIENGESELLSCHAFT KOHLE, M.B.H.,
Plaintiff,

VS.

SHELL OIL COMPANY,
Defendant.

FINAL JUDGMENT UNDER RULE 54(b)

The Court having made various rulings on summary judgment, and having expressly determined that there is no just reason for delay, it hereby revokes the denial of Plaintiff's Motion for Entry of Final Judgment in its Order of September 28, 1995 and directs entry of this final judgment on the matters set forth below:

1. Plaintiff's claim of infringement of claims 1-6 and 14 of U.S. Patent 4,125,698 by defendant's polypropylene operations is dismissed, such patent claims being invalid under 35 U.S.C. 102(b).

2. There is no claim before the Court raising the question of whether any of defendant's polybutylene operations infringe U.S. Patent 4,125,698.

3. There is no claim before the Court raising the question of whether any of defendant's polymerization operations infringe claim 13 of U.S. Patent 4,125,698.

All proceedings herein are stayed, so long as plaintiff takes a timely appeal from this judgment, until the disposition of such appeal. The parties shall move to lift the stay within ten (10) days from the date that the appeal is concluded.

Dated October 10, 1995

/s/ Vanessa D. Gilmore
United States District Judge

[Entered Oct. 11, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

Civil Action No. H-93-3267

STUDIENGELSELLSCHAFT KOHLE, M.B.H.,
Plaintiff,

versus

SHELL OIL COMPANY,
Defendant.

ORDER

The orders of August 31, 1995 and September 28, 1995 involve a controlling question of law as to which there is a substantial ground for differences of opinion. An immediate appeal thereof may materially advance the ultimate determination of the litigation.

Accordingly, this Court certifies the following question of law for interlocutory appeal under 28 U.S.C. § 1292(b):

Where the Court has found the relevant patent claims invalid, may the Licensor recover damages for breach of contract for past royalties due on processes allegedly covered by such claims, from the date of the alleged breach until the date that the Licensee first challenged the validity of the claims.

The Clerk shall enter this Order and provide a copy to all parties.

SIGNED this 10th day of October, 1995.

/s/ Vanessa D. Gilmore
VANESSA D. GILMORE
United States District Judge

NOTE: Pursuant to Fed. Cir. R. 47.6, this order is not citable as precedent. It is a public record.

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

Miscellaneous Docket No. 451

STUDIENGESELLSCHAFT KOHLE, m.b.H.,
Plaintiff-Respondent,

v.

SHELL OIL COMPANY,
Defendant-Petitioner.

On Petition for Permission to Appeal

96-1079

STUDIENGESELLSCHAFT KOHLE, m.b.H.,
Plaintiff-Appellant,

v.

SHELL OIL COMPANY,
Defendant-Appellee,

On Motion to Consolidate

Before PLAGER, *Circuit Judge*, NIES, *Senior Circuit Judge*, and RADER, *Circuit Judge*.

PLAGER, *Circuit Judge*.

ORDER

Shell Oil Company petitions for permission to appeal the orders certified by the United States District Court for the Southern District of Texas as involving a controlling question of law as to which there is a substantial ground for difference of opinion and for which an immediate appeal may materially advance the ultimate termination of the litigation. 28 U.S.C. § 1292(b),(c)(1). Studiengesellschaft Kohle, m.b.H. (SGK) states that it does not oppose the petition. SGK notes that it has appealed another portion of the case, appeal no. 96-1079, certified by the district court pursuant to Fed. R. Civ. P. 54(b). SGK moves for consolidation of the two appeals and for the court to set forth a briefing schedule.

Briefly, SGK and Shell entered into a licensing agreement concerning Shell's manufacture of polypropylene in exchange for royalties. Shell thereafter developed a new polymerization process and it began production under this process. SGK sued Shell for infringing its patent and for breach of contract, alleging that Shell used SGK's patented process in the new polymerization process and that Shell underreported its production and sale of polypropylene and failed to pay royalties under the licensing agreement.

Shell moved for summary judgment of invalidity and noninfringement. On August 31, 1995, the district court granted Shell's motion for summary judgment of invalidity, determining that SGK's patent was invalid as anticipated by prior art. The district dismissed SGK's breach of contract claim and it concluded that SGK's infringement claim was moot.

Turning to SGK's argument that it was entitled to damages for the period following execution of the licensing agreement and until the invalidity determination, the district court concluded that some circuit courts have held that under equity a licensor may recover damages for breach of contract for past royalties earned before and

until the validity of the underlying patent is challenged. The district court noted that this court has not addressed directly the issue of damages for such royalties. *See, e.g., RCA Corp. v. Data General Corp.*, 887 F.2d 1056 (Fed. Cir. 1989). The district court thus concluded that current law "does not prohibit a licensor from recovering damages sustained from the breach of a licensing agreement where the validity of the underlying patent was not challenged until after the breach allegedly occurred." Lastly, the district court ordered that trial proceed on this issue.

Shell moved for reconsideration of the August 31 order, and SGK moved for entry of a final judgment. On September 29, 1995, the district court denied both motions, but concluded that an interlocutory appeal under § 1292(b) would be appropriate concerning whether "SGK is entitled to seek past royalties for processes covered by the invalid claims." On October 11, 1995, the district court set forth the following as the controlling question of law:

> Where the Court has found the relevant patent claims invalid, may the Licensor recover damages for breach of contract for past royalties due on processes allegedly covered by such claims, from the date of the alleged breach until the date that the Licensee first challenged the validity of the claims.

In a second order issued on October 11, the district court vacated its earlier denial of SGK's motion for entry of a final judgment and directed entry of final judgment under Fed. R. Civ. P. 54(b) with regard to the summary judgment of invalidity. On October 26, 1995, SGK appealed, appeal no. 96-1079.

This court makes its own determination whether it will accept an interlocutory appeal pursuant to § 1292(b), (c)(1). *See In re Convertible Rowing Exerciser Patent Litigation*, 903 F.2d 822 (Fed. Cir. 1990). Such a ruling is within this court's complete discretion. *Id.*

We conclude that the first October 11 order meets the criteria of § 1292(b), (c)(1) and that permissive appeal is warranted. The issue that arises in this petition encompasses a controlling question of law and is appropriate for immediate appeal pursuant to § 1292(b), (c)(1). Further, both parties and the district court request that we accept this appeal.

Accordingly,

IT IS ORDERED THAT:

(1) Shell's petition for permission to appeal is granted.

(2) SGK's motion for consolidation is granted.

(3) After Shell's appeal is docketed, SGK will be designated the appellant and Shell will be designated the cross-appellant. The briefing schedule will be computed in accordance with the filing date of Shell's appeal.

Date November 29, 1995

FOR THE COURT

/s/ S. Jay Plager
S. JAY PLAGER
Circuit Judge

cc: Arnold Sprung, Esq.
cc: John D. Norris, Esq.

[Filed Jun. 27, 1997]

UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

96-1079,-1200

STUDIENGESELLSCHAFT KOHLE, M.B.H.
Plaintiff-Appellant,

v.

SHELL OIL COMPANY.
Defendant/Cross-Appellant.

ORDER

A combined petition for rehearing and suggestion for rehearing in banc having been filed by the APPELLANT, and a response thereto having been invited by the court and filed by the CROSS-APPELLANT, and the petition for rehearing having been referred to the panel that heard the appeal, and thereafter the suggestion for rehearing in banc and response having been referred to the circuit judges who are in regular active service,

UPON CONSIDERATION THEREOF, it is

ORDERED that the petition for rehearing be, and the same hereby is, DENIED and it is further

ORDERED that the suggestion for rehearing in banc be, and the same hereby is, DECLINED.

The mandate of the court will issue on July 7, 1997.

FOR THE COURT
JAN HORBALY
Clerk

Dated: June 27, 1997

By /s/ Alex Van Veen
ALEX VAN VEEN
Staff Law Clerk

cc: Arnold Sprung
cc: John D. Norris

[Filed Mar. 23, 1993]

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

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93 Civ. 1868

STUDIENGESELLSCHAFT KOHLE MBH,
Plaintiff,

v.

SHELL OIL COMPANY,
Defendant.

COMPLAINT

Claim 1—Breach of Contract

1. Jurisdiction is conferred on this court by 28 U.S.C. § 1332. The amount in controversy is in excess of $50,000, exclusive of interest and costs. Venue is appropriate under 28 U.S.C. § 1391(a).

2. Plaintiff, Studiengeseilschaft Kohle mbH ("SGK"), is a German corporation having its principal place of business at Kaiser-Wilhelm-Platz 1, D-4330 Mülheim/Ruhr 1, Federal Republic of Germany.

3. Defendant, Shell Oil Company, is a Delaware corporation, doing business in New York, which, upon information and belief, has its principal place of business at One Shell Plaza, Houston, Texas 77252.

4. On or about March 7, 1974, SGK entered into an agreement with defendant (effective as of March 7, 1973) granting defendant permission to use SGK's patented in-

ventions in the field of polypropylene manufacture in exchange for the payment of royalties. This agreement has been supplemented and amended, from time to time, by the parties.

5. Under the agreement, as supplemented and amended, defendant has had the right for the past few years to manufacture up to 300 million pounds of polypropylene per year, using SGK's patented inventions, without payment of royalty, but it must pay a royalty of 1.5% of the net selling price of all such polypropylene in excess of 300 million pounds per year.

6. Defendant has materially breached the agreement by failing to pay agreed-upon royalties for its production in excess of 300 million pounds of such polypropylene per year.

Claim 2—Patent Infringement

7. Jurisdiction is conferred on this court by 28 U.S.C. §§ 1331 and 1338. Venue is appropriate under 28 U.S.C. §§ 1400 and 1391(c).

8. Plaintiff repeats and realleges ¶¶ 2-6 of this complaint.

9. Defendant has been and is using one or more processes claimed in plaintiff's U.S. Patent 4,125,698 to manufacture polypropylene.

10. In view of defendant's breach set forth above, SGK owes defendant no duty to forbear from bringing a claim for patent infringement. SGK elects to treat defendant's manufacture of polypropylene as an infringement of plaintiff's U.S. Patent 4,125,698.

11. In view of defendant's breach, SGK has also sent defendant a notice of termination in accordance with the terms of the 1973 agreement, as supplemented and amended. Unless Shell cures its breach during the next 60 days, the agreement between the parties is, in any event, terminated.

12. Upon information and belief, defendant's infringement is willful and defendant will continue its infringement, to the irreparable injury of plaintiff, unless enjoined by this Court.

Claim 3—Declaratory Judgment Claim

13. Plaintiff repeats and realleges ¶¶ 1-12 of the complaint.

14. This is a declaratory judgment claim, alleged in the alternative, should the Court determine that SGK's claim of patent infringement is not yet ripe. In such event, defendant's actions threaten infringement of the 4,125,698 patent in suit in the near future.

15. A case of actual controversy exists between the parties as to whether defendant's commercial polypropylene processes come within the claims of SGK's U.S. Patent 4,125,698.

16. Despite demands by SGK that defendant pay for its polypropylene production under the claims of this patent, defendant has refused to do so.

17. SGK has given defendant reasonable apprehension that a suit would be forthcoming by repeatedly urging that defendant should pay for its use of the '698 patent in connection with its continuing polypropylene production.

WHEREFORE, plaintiff requests the following relief:

1. Judgment declaring that the 1973 license agreement between the parties, as amended and supplemented, has been breached by Shell;

2. An award of damages suffered by SGK as the result of such breach;

3. Judgment that defendant's processes infringe SGK's U.S. Patent 4,125,698;

4. Judgment declaring that the license agreement between the parties, as amended and supplemented, is terminated;

5. Damages for patent infringement, from and after the date of this action, and the trebling of such damages for willful infringement;

6. An injunction against continued infringement of U.S. Patent 4,125,698 by defendant, its agents, servants and employees, and all those acting in concert with them;

7. A declaratory judgment that even if SGK's claim of patent infringement is not already ripe, defendant's polypropylene process will, in the near future, constitute infringement of the '698 patent in suit;

8. An injunction against such threatened infringement;

9. Interest, costs, reasonable attorneys fees, and such other and further relief as the Court may deem just.

STUDIENGESELLSCHAFT KOHLE MBH

By: /s/ Arnold Sprung, Esq.

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Attorneys for Plaintiff

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

Civil Action No. 93 Civ. 1868 (PKL)

STUDIENGESELLSCHAFT KOHLE MBH,
Plaintiff,

v.

SHELL OIL COMPANY,
Defendant.

ANSWER AND COUNTERCLAIM OF DEFENDANT SHELL OIL COMPANY

Shell Oil Company ("Shell") responds to the complaint of Studiengesellschaft Kohle MbH ("SGK") as follows:

Claim 1—Breach of Contract

1. Shell admits the allegations of paragraph 1.

2. Shell admits the allegations of paragraph 2.

3. Shell admits the allegations of paragraph 3.

4. Shell admits the allegations of paragraph 4.

5. Shell admits that it has had the right to manufacture up to 300 million pounds of polypropylene per year without payment of royalty. Shell denies that any royalty is due for any polypropylene made in excess of 300 million pounds per year.

6. Shell denies the allegations of paragraph 6.

Claim 2—Patent Infringement

7. Shell admits the allegations of paragraph 7.

8. Shell repeats and reasserts its responses to paragraphs 2-6.

9. Shell admits that it produces polypropylene using a catalyst pretreated with diethyl aluminum chloride. Royalties have been paid for the production of any such polypropylene in excess of 300 million pounds per year in accordance with the 1973 agreement, as amended. Shell denies that its remaining polypropylene production is within the valid scope of any claim of U.S. Patent 4,125,698.

10. Shell denies that there has been any breach by Shell and that SGK does not owe Shell a duty to forebear from bringing a claim of patent infringement. Shell admits SGK is attempting to treat Shell's polypropylene manufacture as an infringement of SGK's U.S. Patent 4,125,698 ("the '698 patent"), but denies that any such infringement has taken place.

11. Shell admits that SGK has sent a letter dated March 23, 1993, to Shell purporting to be a notice of termination in accordance with the terms of the 1973 agreement, as supplemented and amended. Shell denies that the letter is an effective notice and that SGK has any basis for terminating the 1973 agreement. Shell further denies that there has been any breach of the 1973 agreement and that any cure is necessary to avoid termination of the agreement.

12. Shell denies the allegations of paragraph 12.

Claim 3—Declaratory Judgment Claim

13. Shell repeats and reasserts its responses to paragraphs 1-12.

14. Shell admits that this claim purports to be a declaratory judgment claim, alleged in the alternative to claim 2 of SGK's complaint. Shell denies the remaining allegations of this paragraph.

15. Shell admits the allegations of paragraph 15.

16. Shell admits that SGK has made demands for royalty payments and that Shell has not met SGK's demands.

Shell denies that it has failed to pay for production of polypropylene produced under the claims of the '698 patent.

17. Shell admits the allegations of paragraph 17.

AFFIRMATIVE DEFENSES

18. SGK's claims for relief are barred by laches.

19. SGK's claims for relief are barred by estoppel.

20. The '698 patent is invalid and unenforceable for failure to comply with the conditions and requirements for patentability set forth in Title 35, United States Code, and the rules, regulations, and law pertaining thereto, including *inter alia*, 35 U.S.C. §§ 101, 102, 103, and 112.

COUNTERCLAIMS

The Parties

21. Plaintiff/counterdefendant SGK is a German corporation having its principal place of business at Kaiser-Wilhelm-Platz 1, D-4330 Mülheim/Ruhr 1, Federal Republic of Germany.

22. Defendant/counterplaintiff Shell is a Delaware corporation having its principal place of business at One Shell Plaza, Houston, Texas 77002.

23. SGK purports to be the owner of record of U.S. Patent 4,125,698 ("the '698 patent").

24. SGK granted Shell a license under its patents in the field of polypropylene manufacture on March 7, 1974 (effective as of March 7, 1973) ("the 1973 license agreement"). The 1973 license agreement was modified in 1979 and 1987.

Jurisdiction

25. In this action, SGK has alleged that Shell by its polypropylene production has infringed the '698 patent.

26. There is a substantial and continuing justiciable controversy between Shell and SGK as to the validity and scope of the claims of the '698 patent and as to whether Shell's polypropylene production infringes any valid claims thereof.

27. By letter dated March 23, 1993, SGK purported to give Shell notice of termination of the 1973 license agreement, as amended. Shell has notified SGK in writing that it believes this notice to be ineffective.

28. Shell has no obligation under the 1973 license agreement, as amended, to pay royalties on the sale of polypropylene made by a method outside the scope of the '698 patent.

29. There is a substantial and continuing justiciable controversy between Shell and SGK as to SGK's right to terminate the 1973 license agreement, as amended.

30. Shell seeks a declaratory judgment to settle the controversy between the parties with respect to the invalidity, unenforceability, and noninfringement of SGK's '698 patent.

31. Shell seeks a declaratory judgment to settle the controversy between the parties with respect to SGK's attempted termination of the 1973 license agreement.

32. Jurisdiction of this court arises under the Federal Declaratory Judgments Act, Title 28, United States Code, Sections 2201 and 2202, and under the laws of the United States concerning actions relating to patents, Title 28, United States Code, Section 1338(a), and under the laws of the United States concerning actions between citizens of a state and citizens of a foreign state, Title 28, United States Code, Section 1332(a).

Claim for Relief

33. The '698 patent is invalid, unenforceable, and void under statutory and decisional law, for failing to satisfy one or more of the provisions for patentability set forth

in Title 35, Part 2, United States Code, and the rules, regulations, and law pertaining thereto, including *inter alia*, the requirements of 35 U.S.C. §§ 101, 102, 103, and 112.

34. If there be any patentable invention in the subject matter of the '698 patent, which Shell denies, the '698 patent nevertheless was not obtained in a manner consistent with the provisions of Title 35, United States Code.

35. Shell has not infringed any valid and/or enforceable claims of the '698 patent.

36. By reason of the proceedings in the Patent and Trademark Office during the prosecution of the application which resulted in the '698 patent, as shown by the file history thereof, SGK is estopped to claim for the '698 patent a construction that would cause the '698 patent to cover or include any Shell process.

37. Pursuant to the terms of the 1973 license agreement, as amended, SGK is entitled to terminate the license for nonpayment of royalties only "in the event of failure of licensee to report and/or make payments due."

38. Shell has reported its polypropylene production to SGK. Shell has paid royalties on its polypropylene production, made using a catalyst pretreated with diethyl aluminum chloride, in excess of 300 million pounds per year in accordance with the 1973 agreement as amended. Shell's remaining polypropylene production is outside the valid scope of any claim of the '698 patent, and therefore, no additional royalties have been due.

39. Shell's nonpayment of royalties on polypropylene production outside the scope of the claims of the '698 patent is not grounds for termination of the 1973 agreement, as amended.

WHEREFORE, defendant Shell demands:

1. Entry of judgment that SGK is without right or authority to threaten or maintain suit against Shell for the alleged infringement of U.S. Patent No. 4,125,698; and

that U.S. Patent No. 4,125,698 be declared invalid, unenforceable, and void in law; and that U.S. Patent No. 4,125,698 is not infringed by Shell.

2. Entry of judgment that SGK's attempted notice of termination of the 1973 license agreement is ineffective and that the 1973 license agreement, as amended, remains in full force and effect.

3. Entry of judgment that SGK's breach of contract claim is barred by the statute of limitations.

4. Entry of judgment that SGK's patent infringement claim is barred by laches and estoppel.

5. Entry of judgment for costs and reasonable attorney's fees incurred by Shell.

AGREEMENT

THIS AGREEMENT, entered into this 7th day of March, 1974, effective as of March 7th, 1973 by and between Studiengesellschaft Kohle m.b.H. as Trustee for the Max Planck Institute of Mülheim/Ruhr, Germany, Lembkestrasse 5, (hereinafter called "LICENSOR"), and SHELL OIL COMPANY, a corporation of Delaware, U.S.A., (hereinafter called "LICENSEE").

WHEREAS, Professor Dr. Dr. h.c. mult. Karl Ziegler (hereinafter called "Ziegler") and LICENSEE have entered into an agreement on December 23, 1964, entitled "Polypropylene Ziegler Patent License Agreement;" and

WHEREAS LICENSOR is the successor to the Patent Rights of Ziegler; and

WHEREAS, in accordance with Article IV of said license, LICENSEE has requested that this License be substituted for the license of December 23, 1964;

NOW, THEREFORE, the following terms and conditions shall be binding upon the parties in lieu of those set forth in said agreement of December 23, 1964.

I. DEFINITIONS

Wherever used in this Agreement, the following terms have the following meaning:

1. The term "Polypropylene" is used herein defining a solid polymer of propylene containing not more than ten (10) mol percent of other monomers, provided said polymers are not elastomers, **or are not used by LICENSEE for the production of elastomers.***

2. The term "Catalyst" or "Catalysts" means any metallic mixed catalyst system (sometimes referred to as a Ziegler-catalyst or Ziegler-catalysts) compris-

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(*) Material set in bold face type was struck through in original.

ing a product formed from compounds of the metals of the sub-groups of Groups IV to VI of the Periodic System and aluminum compounds having the general formula RAlR'R", in which R represents hydrogen or a hydrocarbon, such as an alkyl or aryl radical, and R' and R", which may be the same or different, represent hydrogen, halogen, a hydrocarbon, such as an alkyl or aryl radical, or a radical of a hydrocarbon derivative, such as for example an alkoxy or aryloxy radical.

3. The term "Process" or "Processes" means any process in which propylene is polymerized in the presence of the Catalyst to Polypropylene.

4. The term "Patent Right" shall include the United States patents and patent applications listed in annexed Schedule A, any patents which may issue on said applications, and any patent or patents which issue on continuation, continuation-in-part, division, or reissue applications based upon any of the said patents or patent applications. It shall also include other of LICENSOR's United States patents and patent applications under which a license would be necessary in order to make propylene polymerization Catalysts and use the same for propylene polymerization and make, use, or sell Polypropylene according to the license hereinafter granted.

5. The term "Elastomer" means a material which at room temperature can be stretched repeatedly to at least twice its original length and upon immediate release of the stress will return with force to its approximate original length.

II. LICENSE GRANT

LICENSOR hereby grants the LICENSEE, effective as of the date above, a non-exclusive License under the Patent Rights to make, use, and sell Polypropylene in the United States, its territories and possessions.

III. DOWN-PAYMENT

In view of past royalties paid by LICENSEE to LICENSOR no further down-payment is required.

IV. ROYALTY

LICENSEE agrees to pay LICENSOR a royalty on all Polypropylene produced and either used or sold by LICENSEE pursuant to the License granted herein as follows:

(a) 1.5% (One point Five Percent) of the net sales for the first Five Million Dollars ($5,000,000) of Polypropylene sold by LICENSEE pursuant to the License granted hereunder in each contract year.

(b) 1.2% (One point Two Percent) of the net sales for the next Five Million Dollars ($5,000,000) of Polypropylene sold by LICENSEE pursuant to the License granted hereunder in each contract year.

(c) 1.0% (One point Zero Percent) of the net sales of all sales in excess of Ten Million Dollars ($10,000,000) of Polypropylene sold by LICENSEE pursuant to the License granted hereunder in each contract year.

The "Net Sales Price" shall constitute the gross sales price in U.S. Dollars of the Polypropylene per se as produced or sold by LICENSEE less normal trade discounts, credits and allowances, and freight and returns.

For the purpose of this Agreement, Polypropylene shall be deemed sold when invoiced or delivered to a customer, whichever shall earlier occur, or when utilized by LICENSEE for the production of finished or semi-finished articles.

Where not invoiced, the Net Sales Price of the Polypropylene produced pursuant to the License herein shall be the fair market price of such Polypropylene.

V. BOOKS OF ACCOUNT AND ROYALTY PAYMENTS

On or before the last day of February, May, August, and November of each calendar year during the life of this Agreement, LICENSEE shall furnish to LICENSOR a written accounting containing a detailed computation of all royalties then due and indicating the quantity of Polypropylene manufactured and either used or sold by LICENSEE in the United States and its territories.

At the time of rendering such accounting, LICENSEE shall pay LICENSOR the amount of royalties due in United States Dollars in Germany or in such other place designated by LICENSOR in writing.

All taxes applicable to payments made to LICENSOR pursuant to this Agreement and deriving therefrom shall be borne by LICENSEE with the sole exception of taxes to be paid by LICENSOR in Germany. LICENSOR agrees, on request of LICENSEE, to provide LICENSEE with a written statement that it is a citizen and resident of the Federal Republic of Germany, that it has no permanent establishment in the United States, and that the payments made by LICENSEE are exempt from the withholding of United States tax at source, under the provisions of Article VIII of the convention between the United States and the Federal Republic of Germany.

For the sole purpose of ascertaining the correctness of accountings rendered by LICENSEE and/or computing royalties due from LICENSEE hereunder, LICENSOR by five days written notice shall have the right to inspect LICENSEE's books during regular business hours through a Certified Public Accountant not objectionable to LICENSEE.

VI. TERM

This Agreement shall remain in full force and effect until the expiration date of the last patent or patents within the Patent Right and which have been utilized by

LICENSEE, but may be terminated by LICENSOR upon sixty (60) days written notice:

(a) In the event of failure of LICENSEE to report and/or make payments due hereunder (unless LICENSEE shall correct such failure during said sixty days);

(b) In the event that bankruptcy or similar proceedings concerning the solvency of LICENSEE shall prevent LICENSEE from effectively complying with any of the provisions of this Agreement.

LICENSEE shall have the right to terminate this Agreement:

(a) On ninety (90) days written notice to LICENSOR in the event of any failure or default by LICENSOR under any of the terms of this AGREEMENT, unless said failure or default shall be corrected within said ninety days;

(b) At any time upon written notice to LICENSOR.

LICENSEE shall, after any termination of this Agreement, render a final accounting for all Polypropylene produced and/or sold up to the actual date of termination, according to the provisions of Paragraph V.

VII. THIRD PARTY RIGHTS AND WARRANTY

LICENSOR makes no representations nor warranties with respect to LICENSEE'S right to produce Polypropylene and/or Catalysts or Catalyst components pursuant to the License granted herein, nor with respect to infringement of third party rights. LICENSOR solely warrants it has the right to grant the License granted herein, and that the Patent Rights as set forth in Schedule A constitute all of its rights under which a License is required from it for the manufacture of Polypropylene with a Ziegler-type catalyst and/or the sale of such product.

VIII. TRANSFER OF BENEFICIAL INTEREST IN PERSONAL DEFENSE

LICENSOR hereby transfers and assigns to LICENSEE during the term of this Agreement a beneficial interest in any personal defenses which it may have with respect to third-party patent rights concerning the subject matter licensed hereunder, and agrees to render reasonable assistance and cooperation to LICENSEE in the assertion of such personal defenses.

IX. MOST FAVORED LICENSEE CLAUSE

If LICENSOR during the life of this Agreement subsequently grants to a third party a license to make, use, and sell Polypropylene in the United States, its territories and possessions under more favorable terms and conditions, LICENSOR agrees to promptly advise LICENSEE thereof. LICENSEE, upon ninety (90) days written notice, shall be entitled to such more favorable provisions, provided that LICENSEE agrees to also accept any less favorable provisions or obligations set forth in such third-party license.

Such more-favorable provisions shall only, however, be applicable for so long as the same are applicable to such third party.

In no case, however, shall any provision of this Article be construed as imposing an obligation on LICENSOR to repay or reimburse LICENSEE for any royalties previously paid or due up to the time of any such modification.

X. REPAYMENT

In no case shall LICENSOR be required to repay or reimburse LICENSEE for any royalties paid or due hereunder.

XI. CONFIDENTIALITY

LICENSOR agrees to maintain in confidence any confidential information which it may receive with respect to the business of LICENSEE pursuant to accounts and/or inspection of books hereunder.

XII. ASSIGNABILITY

This Agreement shall be freely assignable by LICENSOR, and shall be freely assignable by LICENSEE to a successor of LICENSEE to substantially the whole business of LICENSEE to which this license pertains. Any other assignment by LICENSEE shall be only made with written consent of LICENSOR and shall only become effective on Assignee's acceptance in writing of all provisions of this Agreement and all of the obligations of the Assignor with respect to this Agreement.

XIII. NOTICES

All notices to be given hereunder shall be sent by cable or registered airmail at their respective addresses set forth hereinafter, provided, however, that either of such addresses may be changed by two weeks written notice hereof to the other party. Any notices given by cable and timely confirmed by airmail shall be effective five (5) days after the cable is sent.

Any notice to LICENSOR shall be addressed to:

Studiengesellschaft Kohle m.b.H.
Lembkestrasse 5
4330 Mülheim/Ruhr
Germany

Any notice to LICENSEE shall be addressed to:

Shell Oil Company
P.O. Box 2463
Houston, Texas 77001
Attention: Patents and Licensing Division

XIV. INTERPRETATION

This Agreement shall be interpreted in accordance with the law of the State of New York, U.S.A.

XV. SCOPE

This Agreement constitutes the full and complete agreement between the parties, and no changes and/or modifications shall be binding unless in writing and signed by the party charged.

The License granted hereunder is the sole license granted, and no further licenses are intended or should be implied. The warranties and representations as set forth herein are the sole warranties and representations made, and no others are implied.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed in their names by their duly authorized representatives as of the date first above written.

STUDIENGESELLSCHAFT
KOHLE m.b.H.

Witness

/s/ [Illegible]

By /s/ [Illegible]

SHELL OIL COMPANY

Witness

/s/ [Illegible]

By /s/ Julius D. Heldman
By /s/ Julius D. Heldman,
Vice President

SCHEDULE A

U.S. Patents:

2,835,689
2,930,808
3,032,574
3,113,115
3,207,770
3,207,772
3,207,773
3,207,774
3,257,332
3,357,967
3,377,332
3,546,133
3,574,138
3,579,493

U.S. Patent Applications:

218,527
514,068
645,548
668,948
716,230
745,998
770,484

AGREEMENT

THIS AGREEMENT, entered into by and between Studiengesellschaft Kohle m.b.H., as Trustee for the Max-Planck-Institut fur Kohlenforschung, of Mulheim/Ruhr, Germany, Lembkestrasse 5, (hereinafter called "LICENSOR"), and Shell Oil Company, a corporation of Delaware, U.S.A., (hereinafter called "LICENSEE"), this 30 day of September, 1979;

WHEREAS, the parties have entered into an agreement on the 7th day of March, 1974, effective as of March 7, 1973, (hereinafter referred to as the " '74 Agreement"), under which LICENSEE has been granted a license under the Patent Rights of Professor Karl Ziegler to make, use and sell Polypropylene in the United States, its territories and possessions, LICENSOR being the successor to these Patent Rights;

WHEREAS, LICENSEE has accounted and paid royalties to LICENSOR under said '74 Agreement, but has questioned its obligation to pay such royalties and LICENSOR'S right to retain the same, and LICENSOR has maintained that such royalties are due and payable to it and are non-returnable; and

WHEREAS, LICENSEE would like to acquire a paid-up license for the production, use and sale of a certain quantity of Polypropylene per year under the Patent Rights as defined in the '74 Agreement;

NOW, THEREFORE, in consideration of the above and in order to settle the above controversy, the parties agree as follows:

1. The Definitions as set forth in the '74 Agreement are applicable herein.

2. LICENSOR hereby grants to LICENSEE, effective January 1, 1979, a fully paid-up license under the Patent Rights to make, use and sell up to four-hundred-fifty (450)

million pounds per calendar year of Polypropylene in the United States, its territories and possessions.

3. For the paid-up license, as set forth above, LICENSEE agrees and hereby obligates itself to pay LICENSOR the sum of one-million-eight-hundred-thousand dollars ($1,800,000), less any regular royalty payments made by LICENSEE to LICENSOR pursuant to the '74 Agreement for sales of Polypropylene made after January 1, 1979.

4. LICENSEE acknowledges the agreement to make payment as set forth above to constitute an unconditional contractual obligation on its part and that the payments made are non-returnable, but may, at its option, make such payments to LICENSOR as follows:

Payment of one-million dollars ($1,000,000), less credits for regular royalty payments made under the '74 Agreement for Polypropylene sales after January 1, 1979, within thirty (30) days of the execution of this Agreement, and payment of the balance of eight-hundred-thousand dollars ($800,000) no later than January 15, 1980.

5. If during any year of the period terminating December 3, 1980, LICENSEE produces a quantity of Polypropylene in excess of four-hundred-fifty (450) million pounds, LICENSEE agrees to pay LICENSOR a royalty of one percent (1%) of the Net Sales of such excess.

6. After December 3, 1980, the parties agree to establish a new royalty rate for yearly production in excess of four-hundred-fifty (450) million pounds, which, however, shall be no greater than the most favorable running royalty rate being paid by any other licensed United States producer of Polypropylene when his production exceeds a paid-up license, if any.

7. LICENSEE represents that its Polybutene production is not covered by the Patent Rights, and LICENSOR accepts this representation and will not challenge the same

for so long as this Agreement has not been breached by LICENSEE.

8. This Agreement shall be interpreted in accordance with the law of the State of New York and shall be controlling where inconsistent with any prior agreements between the parties, including the '74 Agreement.

9. This Agreement does not resolve any conflict between the parties arising from the granting of a license by Professor Dr. Karl Ziegler to Diamond Shamrock Corporation.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed in their names by their duly authorized representatives as of the date first written above.

STUDIENGESELLSCHAFT
KOHLE m.b.H.

By: /s/ [Illegible]

SHELL OIL COMPANY

By: /s/ [Illegible]
General Manager

AGREEMENT

THIS AGREEMENT, entered into this 6th day of July, 1987, by and between Studiengesellschaft m.b.H., as Trustee for the Max-Planck-Institut für Kohlenforschung, of Lembkestrasse 5, Mülheim/Ruhr, Federal Republic of Germany, (hereinafter "SGK"), and Shell Oil Company, a corporation of Delaware, U.S.A., (hereinafter "SHELL");

WHEREAS, the parties are involved in Civil Action No. H-86-4290 in the United States District Court for the Southern District of Texas, entitled *Shell Oil Co. v. Studiengesellschaft Kohle m.b.H., as Trustee for the Max-Planck-Institute for Coal Research, of Mülheim/Ruhr, Germany*, and are desirous of settling said litigation and the controversies between the parties reflected thereby.

NOW, THEREFORE, the parties agree as follows:

1. SGK'S Notice of Cancellation of the agreement between the parties of March 7, 1974 and September 30, 1979 is withdrawn, and the parties agree that said agreements are in full force and effect, except to the extent as modified herein.

2. SHELL agrees to pay SGK a one-point-five percent (1.5%) royalty on net sales of Polypropylene (i.e. solid polymers of propylene containing not more than twenty five (25) mol percent of other monomers, provided said polymers are not elastomers) produced in excess of 450 million pounds per year, utilizing a catalyst with a heavy metal component as defined in claim 1 of the '698 patent, such as a titanium chloride-containing component, which is contacted with a compound having the formula RR'AlX, as defined in claim 1 of the '698 patent. The parties agree that this shall establish the new royalty rate as set forth in Article 6 of the September 30, 1979 agreement.

3. Upon execution of this Agreement, SHELL shall pay SGK the sum of Two Million Dollars ($2,000,000), which shall be non-returnable, but which shall be fully creditable

against the royalties due and payable pursuant to Article 2 above.

4. SHELL agrees to render accountings pursuant to Article V of the March 7, 1974 agreement, except:

(a) the accounting shall be rendered on an annual basis as of December 31 of each year within sixty (60) days of such date.

(b) SHELL shall render an initial accounting as of August 1, 1987, which shall include all yearly production in excess of 450 million pounds which occurred prior to 1987.

(c) On August 1 of each year, beginning on August 1, 1988, SHELL shall make an estimated royalty payment on the production in excess of 450 million pounds for half-year (January through June) period.

(d) With each yearly accounting rendered, SHELL shall specify the amount of Polypropylene produced which it considers as falling outside of the license and shall provide SGK, in confidence, with sufficient information to allow SGK to independently evaluate whether or not said production is, in fact, outside of the scope of the license.

5. Article XII of the March 7, 1974 agreement is modified by the following additions:

> "LICENSEE shall furthermore have the right to assign any portion of its 450 million pound per year paid-up capacity to a purchaser of a manufacturing plant to which the license applied. The assigned paid-up capacity, however, shall not exceed the actual production capacity of the plant in question at the time of its purchase."

6. Civil Action No. H-86-4290, including the Complaint and Counterclaim, shall be dismissed, with prejudice, with each party paying its own costs. The parties shall cause their attorneys to enter into and file an appropriate stipulation to effect this.

IN WITNESS THEREOF, the parties have caused this Agreement to be executed in their names by their duly authorized representatives.

STUDIENGESELLSCHAFT
KOHLE M.B.H.

By: /s/ [Illegible]

SHELL OIL COMPANY

By: /s/ [Illegible]

(2)

No. 97-533

Supreme Court, U.S.
FILED
OCT 27 1997
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

SHELL OIL COMPANY,

Petitioner,

v.

STUDIENGESELLSCHAFT KOHLE m.b.H.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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15pp

Rule 29.6 Statement

Respondent, Studiengesellschaft Kohle m.b.H. ("SGK"), acts a trustee for the Max Planck Institute for Coal Research. Respondent has no other parent or subsidiary companies.

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Blonder-Tongue Lab., Inc. v. Univ. of Ill. Found., 402 U.S. 313 (1971) 8

Bristol Locknut Co. v. SPS Technologies, Inc., 677 F.2d 1277 (9th Cir. 1982) 4

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Compco Corp. v. Day-Brite Lighting, Inc., 376 U.S. 234 (1964) 8

Crane Co. v. Aeroquip Corp., 356 F. Supp. 733 (N.D. Ill. 1973) 6

Hull v. Brunswick Corp., 704 F.2d 1195 (10th Cir. 1983) 4, 5

PPG Industries, Inc. v. Westwood Chemical, Inc., 530 F.2d 700 (6th Cir. 1976) 4

Kraly v. National Distillers & Chemical Corp., 502 F.2d 1366 (7th Cir. 1974) 5, 6, 7

Lear, Inc. v. Adkins, 395 U.S. 653 (1969) 1, 3, 7, 8, 9, 10

Rite-Nail Packaging Corp. v. Berryfast, Inc., 706 F.2d 933 (9th Cir. 1983) 4

Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225 (1964) 8

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Studiengesellschaft Kohle mbH v. Northern Petrochemical Co., 784 F.2d 351 (Fed. Cir. 1986) 1

Westinghouse Elec. & Mfg. Co. v. Formica Insulation Co., 266 U.S. 342 (1924) 8

Statutes and Rules

28 U.S.C. § 1292(b) 6

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Brief in Opposition to Petition for Writ of Certiorari

I. Summary of Reasons for Denying the Writ

A. The decision below, on the question presented, is not in conflict with the decision of any other United States court of appeals. To the contrary, it is in accord with the decisions of four other courts of appeal.

B. The decision below remanded this action to the district court for trial on various issues. Since petitioner has offered additional defenses to respondent's royalty claim, any decision of this court, on the question presented, may turn out to be no more than *dictum* in this action.

C. The decision below correctly applied the law. Nothing in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), is to the contrary.

II. Counterstatement of the Case

Petitioner Shell's polypropylene patent license was amended in 1979 to provide Shell with a paid up license under U.S. Patent 4,125,698 to the extent of 450 million pounds of polypropylene per year. Petitioner's Appendix ("App.") 59a at ¶2. After a decision upholding the patent against various challenges to its validity, *Studiengesellschaft Kohle m.b.H. v. Northern Petrochemical Co.*, 784 F.2d 351 (Fed. Cir. 1986), and an injunction entered thereon, Shell sought and obtained a further license from SGK in 1987 on sales beyond its paid up amount in exchange for an agreement to pay a 1.5% running royalty. App. 62a at ¶2.

In an effort to insure that Shell would report on all its polypropylene sales above the paid up amount, and promptly advise licensor of the details of any polypropylene catalyst and process that Shell believed fell outside the license, the parties additionally agreed, in the 1987 agreement, that:

> "With each yearly accounting rendered, SHELL shall specify the amount of Polypropylene produced which it

> considers as falling outside of the license and shall provide SGK, in confidence, with sufficient information to allow SGK to independently evaluate whether or not said production is, in fact, outside of the scope of the license." App. 63a at ¶ 4(d).

For the next several years, Shell's accountings and royalty payments reflected the fact that all of its polypropylene production came within the license. At no time did Shell advise licensor that it was selling any polypropylene "which it consider[ed] as falling outside the license". Nor did Shell provide licensor with any process information.

But in 1992, when Shell was specifically asked for confirmation that it was reporting on all of its polypropylene, it conceded that it was not. It had been repeatedly breaching its agreement by failing to fully report. App. 11a. Needless to say, it had paid no royalties on the unreported polypropylene. For the first time, Shell explicitly refused to pay such royalty. Its license was, therefore, canceled, and this suit was brought in 1993.

The suit claims, *inter alia*, polypropylene royalties going back to 1987 for Shell's failure to account and pay full royalties while the license was in place, plus damages for patent infringement from the time of cancellation. In its Answer, Shell submitted its first challenge to the validity of the licensed patent. In 1995, the licensed patent expired.

In the district court, Shell moved for summary judgment of invalidity. The district court held that claims 1-6 and 14 of the '698 patent were invalid. It also held that licensor's claim for royalties could go forward, regardless of the validity of the patent claims.

The Federal Circuit Court of Appeals affirmed both rulings. On the latter, the court pointed out that under state contract law, "[n]othing in this license made payment of royalties contingent upon the validity of the '698 patent." App. 11a.

Indeed, it would be an "injustice" to allow "Shell to exploit the protection of the contract and patent rights and then later to abandon conveniently its obligations under those same rights." App. 14a.

The Federal Circuit recognized that federal patent law and policy might, in certain limited circumstances, supersede state contract law. App. 12a. But under the facts of this case, the court held it did not. Such federal patent law and policy did not prevent the licensor here from recovering royalties through "the date Shell first challenged the validity of the claims." App. 13a. Moreover, Shell's delay in challenging validity was more likely to "frustrate federal patent policy than enforcement of the contract." App. 14a.

> "By abrogating its notification duty, Shell delayed a timely challenge to the validity of the '698 patent and postponed the public's full and free use of the invention of the '698 patent. Shell enjoyed the protection of the license from 1987 until SGK became aware of the Sea-drift Process. [It was only then that Shell sought] . . . the protection of the *Lear* policies it flaunted for many years." App. 14a.

The court concluded that Shell must abide by its contract and pay such royalties as could be shown to have accrued prior to the date of its challenge to validity. App. 14a-15a. In so ruling, it joined four other circuits that have addressed the same issue. *Ibid.*

III. Reasons for Denying the Writ

A. The Writ Should Be Denied Because the Decision Below is in Accord With the Decision Of Every Other Circuit That Has Addressed the Issue

This court's limited resources are normally directed to cases where there is a conflict among the circuits or between federal and state court decisions. *See* Sup. Ct. R. 10. But here, there is no conflict. The decision below is in accord with those of the four other circuits which have addressed the question. *Hull v. Brunswick Corp.*, 704 F.2d 1195, 1203-04 (10th Cir. 1983); *Rite-Nail Packaging Corp. v. Berryfast, Inc.*, 706 F.2d 933, 936-37 (9th Cir. 1983); *Bristol Locknut Co. v. SPS Technologies, Inc.*, 677 F.2d 1277, 1282-83 (9th Cir. 1982); *American Sterilizer Co. v. Sybron Corp.*, 614 F.2d 890, 896-97 (3d Cir. 1980); *PPG Industries, Inc. v. Westwood Chemical, Inc.*, 530 F.2d 700, 703-07 (6th Cir. 1976).

As those courts have explained:

> "Bristol Locknut [the licensee] received substantial benefit under the licensing agreement. Consequently, Bristol Locknut's obligation to pay the full royalties owed under the contract continued until it challenged the validity of the patents. To hold otherwise, under these facts, would be inequitable and would undermine federal patent law policy." *Bristol Locknut*, 677 F.2d at 1279.
>
> "The actions of PPG in the present case in ceasing the payment of royalties [without challenging validity] were not of the type to prompt an early adjudication of invalidity. It is for this reason . . . that the liability of PPG for royalties did not cease as of the date of termination of payments." *PPG Industries*, 530 F.2d at 706.
>
> "If licensees are permitted to suspend royalty payments without notifying licensors that the reason for the suspension is to question the validity of the patents, they

> will be subject to a . . . temptation to forestall validity litigation." *Hull*, 704 F.2d at 1203.
>
> "[T]he key issue is whether a prompt challenge to the patent follows the licensee's suspension of royalty payments." *American Sterilizer*, 614 F.2d at 897.

In operation, the "challenge rule" applied by the five circuit courts encourages early patent validity determinations in two ways:

* The licensee is encouraged to analyze validity of the licensed patent and, if he finds the patent to be invalid, to discontinue his royalty payments and promptly challenge validity. If he is sued for royalties, he can escape payment for all royalties which might accrue after the challenge, assuming that he can succeed in showing patent invalidity.

* The patentee is encouraged to promptly bring suit where his patent's validity has been challenged and royalties stopped. He knows that there is no point in waiting for unpaid royalties to mount up. The licensee has challenged validity; if he can prove invalidity, a claim for royalties back to the date of the challenge will be fruitless.

Petitioner urges that the Third, Sixth, Ninth, Tenth and Federal Circuits are arrayed against the Seventh in view of the latter's decision in *Kraly v. National Distillers & Chemical Corp.*, 502 F.2d 1366 (7th Cir. 1974). But *Kraly* is not at all to the contrary. It simply decides a different issue.

In *Kraly*, despite a holding of patent invalidity, the district court awarded the patentee four quarters of back royalties, the royalties which accrued until the licensee " 'had repudiated the license agreement and assumed the risk of being found liable for infringing. . . .' " *Id.* at 1372. The Court of Appeals affirmed, approving the decision as an "appropriate

use of judicial power to enforce the terms of a licensing agreement during the period prior to an adjudication of invalidity in which both parties benefited from the agreement." *Ibid.* No issue was raised on whether the timing of the licensee's challenge to validity had any impact on the recoverability of royalties.[1]

B. The Writ Should Be Denied as the Question Presented May Never Have to be Reached in the Instant Action

The issue presented was decided below on an interlocutory appeal under 28 U.S.C. § 1292(b). App. 11a. After its decision, the Federal Circuit remanded, *inter alia*, for a determination of whether, in fact, any royalties were owed. App. 15a. The court also denied petitioner's motion to stay the mandate pending this petition for certiorari. Petition at 2.

Since then, the District Court has denied petitioner's motion for a stay of proceedings pending the filing and resolution of the instant petition for certiorari, and it has issued a further scheduling order providing for trial of this action in February 1998.

Shell has already advised that it will defend against the royalty claim, at trial, on the theory that it has not infringed. Should it prevail on this ground, the district court will never be required to address the question presented herein. Put

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[1] Shell also relies on the district court decision in *Crane Co. v. Aeroquip Corp.*, 356 F. Supp. 733 (N.D. Ill. 1973). But in *Crane*, the patentee was not asserting the challenge rule of the five circuit courts (those decisions had not yet been rendered), but rather a rule that would have precluded any cut-off of royalty accrual until there was a *lawsuit* in which validity was challenged. *Id.* at 740.

The court pointed out that if *this* rule were the law, it would not encourage early adjudication of validity. "[T]he patentee could simply wait until the patent expires and sue for all royalties not paid 'prior' to the litigation." (*Ibid.*) The only thing the licensee could do to prevent such a result would be to "bring a suit for a declaratory judgment that the patent is invalid." *Ibid.*

differently, the review sought herein is on an issue which may never have to be reached in this action.

C. The Writ Should Be Denied Because the Decision Below Correctly Applied the Law—Nothing in *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969), is to the Contrary

A patent license is basically nothing more than a licensee's promise to pay royalties in exchange for a patentee's promise to forbear from doing what the patent law otherwise entitles him to do, namely sue for infringement and potentially collect damages based on a tort standard, sometimes trebled, along with an injunction.

In the instant case, the licensee, Shell, has received substantial benefit under its license, including the agreed upon freedom from an infringement claim during the period from 1987 until 1993. Accordingly, Shell owes all royalties accrued in this period which have not been paid. Since nothing in the parties' agreement warranted the validity of the licensed '698 patent, or otherwise made the payment of royalties contingent upon patent validity, under state contract law, royalties are payable without regard to the validity of the licensed patent. App. 11a-12a.

Under state contract law, for a licensee to avoid royalties for any period, it would have to show that it had, before that period started, unequivocally given up its freedom from an infringement suit by returning to the same unprotected status as an infringer. It could do this by showing it terminated the agreement or, where recognized by the Court's jurisprudence, by showing it "repudiated" the protection of the license. *See, e.g., Kraly, supra*; *Bahamas Paper Co. v. Imperial Packaging Corp.*, 58 F.R.D. 355, 357 (S.D.N.Y. 1973).

But Shell plainly did neither in the instant case. Instead, it avoided exposure on the production it was not paying for by disregarding the provision of its license that expressly required it to tell its licensor, with each annual royalty report,

of any polypropylene it considered as falling outside of the license.

Shell received freedom from tort suit during the period from 1987 to 1993. Under state contract law, it owes all royalties which accrued during that period, without regard to patent validity. *See* App. 11a-12a. Indeed, Shell concedes as much. Petition at 18.

There is no federal patent statute that applies here, and the only precedent of this court even remotely relevant is *Lear, Inc. v. Adkins*, 395 U.S. 653 (1969).[2] But nothing in *Lear* requires that Shell's obligations under state contract law must be abrogated. *Lear* merely requires that the licensee be permitted to challenge patent validity at an early time, so that the public stands to benefit if there is a determination of invalidity.

In *Lear*, the licensee of a patent application discovered apparently anticipatory prior art in 1957 and promptly advised the licensor that since no valid patent should issue on the application, it would refuse to pay further royalties on the bulk of its products. *Id.* at 659. Put differently, it discontinued royalty payments and, at the same time, challenged validity. In 1960, a patent did issue on the application. *Id.* at 660.

In a suit for royalties, the California Supreme Court ruled that the licensee had no contractual right to terminate its

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[2] The other cases cited by Shell are inapposite. For example, *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225 (1964) and *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234 (1964) deal with the power of a state to set up a mini patent system under its unfair competition laws. *Blonder-Tongue Lab., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313 (1971) deals with the applicability of collateral estoppel in a patent case. *Brulotte v. Thys Co.*, 379 U.S. 29 (1964) deals with the propriety of requiring a licensee to pay royalties accruing after the expiration of a patent. *Westinghouse Elec. & Mfg. Co. v. Formica Insulation Co.*, 266 U.S. 342 (1924), deals with an assignor estopped to deny validity and the equitable remedy fashioned by the court to ameliorate that estoppel.

license and that it could not avoid payment of royalties by showing that the licensed patent was invalid. In short, despite its early challenge to validity, the licensee was estopped to deny validity of the licensed patent. *Id.* at 661, 656. The court reinstated a jury verdict in favor of the licensor for back royalties.

In reversing, this Court held that in view of federal patent policy, state contract law must give way to the following extent:

1. Licensees are not estopped from contesting patent validity. *Id.* at 669-71.

2. Licensees are not required to continue paying royalties during the time they are challenging patent validity in the courts. *Id.* at 673.

3. The licensee before it was entitled to avoid payment of all patent royalties which accrued after its 1957 challenge to validity, if it could prove the patent was invalid. *Id.* at 674.

But none of these holdings is contrary to that of the Federal Circuit in the instant case. Shell was certainly permitted to challenge patent validity herein. App. 5a-8a. Further, the parties' license was never construed to require that Shell had to pay royalties during the time it was challenging patent validity in the court. Finally, since Shell proved claims 1-6 and 14 invalid, it was entitled to avoid payment of all patent royalties which accrued under such claims after it first challenged validity. App. 11a-15a.

Moreover, as confirmed by the Third, Sixth, Ninth and Tenth Circuits, the court below properly declined to extend *Lear*. It refused to supersede additional state contract rules in the name of federal "public policy". This would be a particularly inappropriate case to extend *Lear*.

1. Shell, unlike the licensee in *Lear*, had a contractual right to terminate, and could have terminated the license agreement

at any time since 1987, so as to avoid further obligations under its license. App. 54a. But Shell chose, instead, to keep silent about its excess production in order to reap the benefits of its license while avoiding a claim by its licensor for royalties. *See* App. 14a.

2. In light of the holding in *Lear*, Shell also had the option of promptly challenging validity so as to bring on a rapid determination of validity. But unlike the licensee in *Lear*, which simultaneously discontinued royalty payments and challenged validity, Shell chose, instead, to delay any challenge to validity, gambling that its licensor would never learn that Shell was exceeding its paid up license. As a result of such delay, the determination of invalidity did not take place in the instant case until 1995, shortly before the '698 patent expired, at a time when it could do little good for the public.

3. Finally, even though Shell's challenge to validity was not prompt, Shell, like the licensee in *Lear*, has nevertheless gained a valuable benefit from its challenge, the right to avoid all royalties which might accrue from and after the date of its challenge.

Conclusion

For each of the above reasons, Shell's petition for a writ of certiorari should be denied.

Respectfully submitted,

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IN THE
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OCTOBER TERM, 1997

SHELL OIL COMPANY,
Petitioner,

v.

STUDIENGESELLSCHAFT KOHLE M.B.H.,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Federal Circuit

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PETITIONER'S REPLY BRIEF

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Shell respectfully submits this reply brief to address the arguments in SGK's opposition, although SGK's opposition is more probative for what it does not say, for what it does not rebut, and for what it does not even try to defend. As shown herein, SGK's opposition mischaracterizes this Court's precedent and the record, and confirms that the Federal Circuit's precedential rule is flawed as a matter of law, policy, and logic.

SUMMARY OF THE REPLY

The reason that Shell's petition should be granted is straightforward. The rule announced by the Federal Circuit in this case—that a patent licensor may still pursue a contract action to recover unpaid license royalties after the licensed patent has been held invalid—is contrary to this Court's precedent, is misguided as a matter of federal patent policy, and is wasteful of scarce judicial resources as a matter of judicial administration. Where a patent licensee withholds royalty payments and is later sued by the licensor, proving invalidity of the licensed patent should remain a complete defense to the licensor's claims for royalty damages under any legal theory.

Just as proof that the licensed patent is not infringed provides a complete defense to a suit for unpaid license royalties, a licensee that satisfies the higher burden of proving that the licensed patent is invalid should obtain an equal benefit. Simply put, once the patent is held invalid, the court should leave the parties where it finds them. Absent fraud, the licensor keeps royalties already paid. At the same time, the licensee is freed from any further liability with respect to the invalid patent. There is no justification for allowing a licensor of an invalid patent to continue to litigate in search of an even greater undeserved windfall.

Presented in this case with a certified legal question of first impression for the Federal Circuit, that court was given the opportunity, as the court with exclusive jurisdiction over appeals arising under the patent laws, to reject an erroneous line of federal decisions stemming from the Sixth Circuit's decision in *PPG Indus., Inc. v.*

Westwood Chem., Inc., 530 F.2d 700, 703-07 (6th Cir.), *cert. denied*, 429 U.S. 824 (1976). Purporting to promote a nonexistent policy of encouraging early challenges to validity, those decisions allowed a licensor to recover unpaid royalties accrued between the time the licensee stopped making full royalty payments and the time that the licensee informed the licensor that the validity of the licensed patent was being challenged. By adopting rather than rejecting the rule created by the *PPG* line of cases, the Federal Circuit's decision has established that arbitrary, wasteful, and erroneous rule as the controlling law in federal district courts.

In doing so, the Federal Circuit violated this Court's landmark decision in *Lear v. Adkins*, 395 U.S. 653 (1969), which eliminated the doctrine of licensee estoppel and held that state contract law cannot provide a basis for recovering unpaid royalties under a license to an invalid patent. Yet, by authorizing SGK to pursue unpaid royalties after the relevant claims of its licensed patent have been held invalid, the Federal Circuit's rule means that licensees, such as Shell, are once again estopped by their license from using invalidity as a defense, at least prior to informing the licensor that its patent is deemed invalid. In practical effect, the Federal Circuit partially overruled *Lear*. Of course, only this Court is empowered to take such action.

I. THE FEDERAL CIRCUIT'S RULE IRRECONCILABLY CONFLICTS WITH THIS COURT'S LANDMARK DECISION IN *LEAR*

Somewhat predictably, SGK's first reason as to why this petition should be denied is its assertion that there is no conflict among the circuits that needs to be remedied. Brief in Opposition ("Opp.") 4-6. Not only is that assertion incorrect, *see* Petition ("Pet.") 27-30, but it completely ignores that the irreconcilable conflict is the one existing between this Court's decision in *Lear* and the line of federal court decisions that have adopted the erroneous "challenge" rule first announced in *PPG*.

Apart from urging that Shell's petition be denied, SGK offers no analysis that supports the Federal Circuit's rule. Instead, SGK merely recites conclusory passages (Opp. 4-5) from the very line of federal cases that Shell's petition demonstrated were wrongly decided in light of *Lear* and thus provide the central basis for granting this petition. SGK made no attempt to rebut Shell's showing that the supposed policy of encouraging early adjudications of patent invalidity is nowhere to be found in *Lear* or any other precedent of this Court. Pet. 24-27. Instead, SGK simply recites that policy as unilaterally announced by the Sixth Circuit in *PPG* as being the dispositive factor and assumes that recitation is enough to outweigh the contrary holdings of this Court.

SGK did not even attempt to rebut Shell's showing why the "benefits" identified by the Federal Circuit as allegedly flowing to licensees, such as Shell, from a license under an invalid patent, are illusory. Instead, SGK simply proclaimed that Shell received a "substantial benefit" in being free from an infringement suit during the period of the license. Opp. 7. However, because Shell never paid royalties for the polypropylene from its Seadrift process, any alleged freedom from suit was nonexistent with respect to that process. Pet. 20-21.

Like the Federal Circuit, SGK tries to justify that court's adoption of the "challenge" rule on grounds that Shell "avoided exposure" by allegedly breaching its contractual duty to inform SGK of the Seadrift production which Shell believed was not covered by the patent claims, and thus not by the license. Opp. 7-8. That alleged reporting breach, however, is not a legitimate basis for the Federal Circuit's ruling that Shell is potentially liable for back royalties, because Shell cured any such breach in accord with the license. *See* Pet. 8 at n.3. Indeed, SGK's breach of contract claim is based solely on Shell's nonpayment of royalties, not on an alleged failure to report its Seadrift production. App. 40a-41a. More importantly, for purposes of the rule of law urged by SGK and adopted by the Federal Circuit, Shell clearly did not avoid any

exposure to liability with respect to the Seadrift process for which Shell never paid royalties.

Contrary to SGK's assertion at Opp. 8, Shell did not concede that an alleged freedom from a "tort suit" rendered Shell liable under state contract law for all royalties that accrued while the Seadrift process was in operation until the license was terminated in 1993. Instead, Shell merely pointed out that if the license were truly not contingent upon patent validity, state contract law would require the licensee to pay all royalties for the entire contract term, whether or not the patent claims were subsequently held invalid—a result that even SGK had already conceded is not the law. *See* Pet. 18. Moreover, by restricting its assertion to alleged freedom from a "tort suit," SGK concedes that Shell had no freedom from a contract suit when royalties were not paid on its Seadrift process. *See* Opp. 8.

At least with respect to the post-challenge period, SGK implicitly agrees that something in *Lear* "requires that Shell's obligations under state contract law must be abrogated." *Id.* In actuality, there is nothing in *Lear* that suggests that a licensee's obligations under state law are only abrogated for the period after an express challenge to validity. That deadline is simply arbitrary, and has the erroneous effect of reinstating licensee estoppel prior to that time. Once a licensee withholds any royalties, the date upon which validity is later challenged should be legally irrelevant.

According to SGK, the artificial deadline reflects that *Lear* "merely requires that the licensee be permitted to challenge patent validity at an early time, so that the public stands to benefit if there is a determination of invalidity." Opp. 8. As demonstrated in Shell's petition, no such deadline or policy is found anywhere in *Lear*, and this Court clearly did not contemplate that post-issuance royalties could be recovered if the patent in *Lear* was held invalid on remand. Pet. 14-17. In explaining its rationale, this Court reasoned that a licensee "will have little incentive to initiate lengthy court proceedings, unless

he is *freed from liability at least from the time he refuses to pay the contractual royalties.*" 395 U.S. at 673-74 (emphasis added).

Moreover, this Court in *Lear* rejected an attempt to enforce a license provision that royalties were to be paid until such time as the patent was held invalid. *Id.* at 673. If such a provision was not enforced in *Lear*, the Federal Circuit clearly erred in allowing an alleged breach of a notice provision to justify recovering past due royalties on invalid patent claims. The mere existence of an ultimately cured breach cannot justify allowing state contract law to enable a licensor to seek past royalties for a license under an invalid patent. Such a result is clearly preempted by federal patent law and policy as repeatedly announced by this Court.

In this case, Shell accepted a license for its older processes and paid millions to SGK in royalties. Shell did not pay royalties on polypropylene made with its Seadrift process based on its belief that the new process was not covered by any claim of the '698 patent. When SGK later sued to obtain royalties on that process as well, Shell was "secure in the knowledge that invalidity may be urged when the patentee-licensor sues for unpaid royalties." *Blonder-Tongue Lab., Inc. v. Univ. of Ill. Found.*, 402 U.S. 313, 346 (1971). Shell did exactly that, proved invalidity by clear and convincing evidence, had that holding affirmed on appeal, and yet now finds itself back in district court with the further burden and task to demonstrate noninfringement. On its face, the Federal Circuit's rule violates the law established by this Court in *Lear* and later confirmed in *Blonder-Tongue*. *See* Pet. 15-16.

In *Cardinal Chem. Co. v. Morton Int'l, Inc.*, 508 U.S. 83, 100-01 (1993), this Court rejected the Federal Circuit's practice of routinely vacating district court decisions on patent validity upon affirming or reaching a finding of noninfringement. In doing so, this Court reiterated its view that "of the two questions, validity has the greater public importance" and noted that "the better practice"

is for district courts to inquire fully into the validity of the patent-in-suit. *Id.* at 100 (quoting *Sinclair & Carroll Co. v. Interchemical Corp.*, 325 U.S. 327, 330 (1945)).

In addition, this Court in *Cardinal* again emphasized "the importance to the public at large of resolving questions of patent validity." 508 U.S. at 100 (citing *Blonder-Tongue*). Yet, here, the Federal Circuit's rule has the effect of penalizing the first party to prove invalidity of the patent claims, purportedly because that party did not do so sooner. This Court should not allow the Federal Circuit to create another misguided rule that encourages defendants and district courts to avoid litigating and resolving the issue of patent validity.

As explained in Shell's petition, if invalidity does not provide a complete defense to a claim for unpaid royalties, licensees will focus their attention on proving non-infringement, whenever possible, because of its lower burden of proof and the ability to gain a complete defense. Pet. 23-24. As in *Cardinal*, the net result of such a rule will be to prolong the life of invalid patents. 508 U.S. at 102. Not only will that not benefit the public, but unlike situations where patent validity at least remains in doubt, the Federal Circuit's rule as announced in this case allows a licensor to seek even greater unwarranted rewards for patent claims that already have been finally adjudicated to be invalid.

II. BY ERRONEOUSLY FOLLOWING ITS OWN DECISION IN *DIAMOND SCIENTIFIC*, THE FEDERAL CIRCUIT IMPERMISSIBLY EQUATED ASSIGNOR ESTOPPEL AND LICENSEE ESTOPPEL AND EFFECTIVELY OVERRULED THIS COURT'S HOLDING IN *LEAR*

SGK's opposition did not even try to defend the Federal Circuit's improper end run around *Lear* based on its inapt reliance on its own decision in *Diamond Scientific Co. v. Ambico, Inc.*, 848 F.2d 1220 (Fed. Cir.), *cert. dism'd*, 487 U.S. 1265 (1988). As Shell pointed out (Pet. 19-20), the Federal Circuit carefully sidestepped *Lear* in reaching its decision in *Diamond Scientific* to

resurrect assignor estoppel, by drawing an explicit distinction between an assignor and a licensee:

> The public policy favoring allowing a licensee to contest the validity of the patent is not present in the assignment situation. Unlike the licensee, who, without *Lear*, might be forced to continue to pay for a potentially invalid patent, the assignor who would challenge the patent has already been fully paid for the patent rights.

848 F.2d at 1224. However, the Federal Circuit conveniently ignored that distinction in the present case when it relied on *Diamond Scientific* to legitimize SGK's contract suit for royalties under a license to an invalid patent—in violation of *Lear*.

Unable to provide any plausible justification for how the Federal Circuit could legitimately distinguish licensee estoppel in *Lear* from assignor estoppel in *Diamond Scientific* and then rely on *Diamond Scientific* to allow a partial return to licensee estoppel in this case, SGK does not even cite or mention *Diamond Scientific* in its opposition. Such conspicuous silence should make it clear to this Court that Shell's petition is well taken and should be granted. On its face, neither the Federal Circuit's legal bootstrapping to avoid this Court's decisions nor its resulting legal conclusion in conflict with this Court's holdings can be supported or condoned.

A fundamental issue underlying this petition is whether federal courts should feel free to ignore or distinguish decisions of this Court as long as they remain in agreement with the result or rationale of the first circuit court to do so. Presumably, this Court expects its decisions to be followed. Thus, the failure of a number of the federal circuits to adhere to this Court's precedent in *Lear* and *Blonder-Tongue* should be a compelling reason to grant Shell's petition in this case, not a reason for denying it and thus allowing licensee estoppel to be reinstated over time in the same manner that the Federal Circuit unilaterally restored assignor estoppel in *Diamond Scientific*.

Shell's petition also provides this Court with the opportunity to clarify whether the privilege of overruling Su-

preme Court decisions related to patent law and announcing federal patent policy remains the province of this Court, or whether the Federal Circuit is now free to do as it pleases when faced with a patent precedent of this Court with which it disagrees. In this case, the Federal Circuit's opinion expressly dismissed this Court's decision in *Lear* as merely a by-product of "tones that echo from a past era of skepticism over intellectual property principles." App. 12a.

In its petition, Shell outlined the Federal Circuit's own summary of its repeated efforts to avoid *Lear* in its decisions prior to this one. Pet. 8-9 at n.4; App. 12a-13a. Up until now, this Court has not been given a chance to review those prior Federal Circuit decisions undermining *Lear*. If this Court is willing to stand idle while one of its leading patent decisions is progressively limited to its facts, as the Federal Circuit has already done by distinguishing or sidestepping *Lear* at every opportunity, then it makes a mockery of this Court's practice of only granting certiorari in cases with widespread significance to the development of the law.

If a landmark opinion such as *Lear* is to be overruled or limited, such action should be taken by this Court, not by the Federal Circuit or by any regional circuit. At a minimum, such bold action by the lower federal courts should be expressly approved by this Court. While Congress created the Federal Circuit in 1982 to bring uniformity to the patent laws, Congress presumably left final review of the Federal Circuit's patent decisions in the hands of this Court for a reason. *See Cardinal*, 508 U.S. at 97 ("the Federal Circuit is not a court of last resort").

In *Lear*, this Court completely eliminated the doctrine of licensee estoppel and recognized that patent invalidity would be a complete defense to a licensor's claim for unpaid royalties. By granting this petition, this Court will be able to reaffirm that the patent issues already decided by its opinions remain the final pronouncements as to federal patent policy unless and until changed by this Court.

III. THE FEDERAL CIRCUIT'S RULING ON THE QUESTION PRESENTED CANNOT BE ALTERED BY THE DISTRICT COURT AND WILL REMAIN THE CONTROLLING PRECEDENT IN PATENT LICENSE CASES UNLESS THIS PETITION IS GRANTED

Finally, SGK resorts to the ploy of all oppositions to petitions for certiorari in arguing that "any decision of this court, on the question presented, may turn out to be no more than *dictum* in this action" because the case has been remanded to the district court for trial on various issues. Opp. 1. More so than in most cases, SGK's argument is utterly misplaced.

The question presented by Shell's petition was certified for appeal under 28 U.S.C. § 1292(b) because it was a controlling question of law whose immediate resolution would prevent the district court from having to conduct an extensive infringement trial unnecessarily. *See* App. 33a. Because the conflict between this Court's decision in *Lear* and the erroneous "challenge" rule created by the post-*PPG* decisions in the regional circuits had never been addressed by the Federal Circuit, that court could have clarified the law and resolved any confusion without the involvement of this Court.

Now that the Federal Circuit has become the latest federal appellate court to deviate from this Court's precedent, the need to resolve correctly and conclusively the legal issue as to whether unpaid license royalties can be recovered by the licensor after the licensed patent is held invalid has not diminished. If anything, it has now become even more critical for this Court to resolve that important legal question now, in this case, once and for all. If the Federal Circuit's decision is allowed to remain the law of the land, district courts across the country will be forced to waste scarce judicial resources adjudicating infringement of patents that have already been held to have no valid scope.

SGK also asserts that "the district court will never be required to address the question presented herein" if Shell

prevails on its defense that it did not infringe invalid claim 1 of the '698 patent. Opp. 6. With all due respect, that assertion is absurd. The question as to whether a district court would have to decide whether royalties are due on the invalid patent is exactly the legal issue that was certified for appeal by the district court, and exactly the issue that has already been decided by the Federal Circuit. On remand, the district court has no ability or discretion to deviate from that mandate. With the relevant claims of the patent already affirmed as invalid, the district court has no choice but to resolve whether SGK's invalid patent was infringed by Shell, unless Shell's petition is granted.

If SGK is actually arguing that this Court should decline to hear Shell's petition at this stage of the case because the district court could still decide on remand that Shell does not owe any license royalties for the "pre-challenge" period in question, that suggestion is disingenuous. If Shell does not or cannot raise this issue after final judgment because it prevailed on noninfringement or any of its other defenses, this Court's best chance to review the erroneous rule mandated by the Federal Circuit's precedential opinion in this case will be lost and all district courts hearing patent cases will be bound by that wasteful rule.

Simply put, a licensor should not be allowed to use state contract law to pursue unpaid royalties after the licensed patent has been held invalid. Shell's petition for writ of certiorari should be granted to make clear that there should *never* be a remand for further proceedings to determine liability for unpaid royalties under a license to an invalid patent.

Respectfully submitted,

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